

United States
Circuit Court of Appeals
For the Ninth Circuit.

EDMUND J. LORD,

Appellant.

vs.

TERRITORY OF HAWAII,

Appellee.

Transcript of Record

Upon Appeal from the Supreme Court of the
Territory of Hawaii.

FILED

SEP 21 1934

PAUL F. O'BRIEN,
CLERK

United States
Circuit Court of Appeals
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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In the Supreme Court of the Territory of Hawaii.

October Term, 1933.

No. 2052

In the Matter of the Income Tax Appeal
of

EDMUND J. LORD

for the year ending December 31, 1930,
First Taxation Division.

APPEAL FROM TERRITORIAL BOARD OF
EQUALIZATION.

AMENDED RETURN

Territory of Hawaii
First Taxation Division, District of Honolulu

INDIVIDUAL INCOME TAX RETURN
For the Twelve Months Preceding January 1,
1931

Form B18

Ext. No.

Date filed

6/18/31

(Sgd.) H. GLASS

filed by (Sgd.) H. W. Camp

Notice of Proposed Change

Identified.....

Jun. 29, 1931

Reported

(Form B9b-409)

Name Edmund J. Lord

Nationality Age 62

Residence c/o Hawaiian Trust Co. Ltd.

Street and number)

Honolulu

Occupation or Profession

(Kind of Business)

By whom employed

(Name of Employer)

Location of Business

(Street and number)

Telephone No..... P. O. Box No.....

Were you married and living with husband or wife on December 31, 1930? no

If not, what was your status on December 31, 1930?.....

If married, give full name of husband or wife.....

How many dependent persons, other than husband or wife, under 18 years of age, or incapable of self-support because mentally or physically defective, were receiving their chief support from you on December 31, 1930? two

State relationship and age of such dependents

mother and daughter

Is this a joint return of husband and wife?.....

If not, state exemption claimed by husband or wife \$.....

Did you file a return last year? yes

At which office? Honolulu

INCOME

1. Salaries, Wages, Commissions, etc.
(State source from which derived)
(a) \$.....
(b)
2. Gross Income from Business or Profession
- 2a. Merchandise Withdrawals from Business
3. Interest on Bank Deposits, Notes, Mortgages,
Corporation Bonds, Government Bonds
(Foreign or Mainland Municipal Public
Utility), etc. 9,969.99
4. Dividends from Corporations not subject to
Territorial Income Tax:
(List name of Corporation)
.....
5. Net Profit from sale of Real Estate, Stocks,
Bonds, etc. (From Schedule B)
6. Gross Rentals derived from sources within
the Territory
7. Income from Partnerships, Fiduciaries, etc.
(Explain in Schedule D):
(State name and address of partnership, etc.)
8. Exempt Income (Deduct in Item 15 below)
- (a) Dividends from Corporations subject to
Territorial Income Tax:
(List name of Corporation) \$406,569.98 see schedule
Pioneer Mill Co. \$580.
Maui Agri. Co. \$1308. E. J. Lord Ltd 408,457.98

(b) Interest on United States, Territorial or Local Government Bonds	2,901.67
(c) Personal Property acquired by Gift or Inheritance (Explain) :	
.....	
9. Other Income (State Nature of Income)	
10. Total Income in Items 1 to 9	
(Carry to Item 18 at Top)	<u>\$421,329.64</u>

DEDUCTIONS

11. Interest paid (Except on indebtedness incurred outside of Territory) :	
(Itemize)	
(a)	1,420.43
(b)	
12. Taxes paid (Except on Property located outside of Territory) :	
(a) Property Taxes (Not including Frontage or Improvement Taxes)	2,790.64
(b) Territorial Income Taxes	
(c) Federal Income Taxes	11,471.17
(d) Other Taxes (Including Licenses—Explain) :	
Auto tax \$86. — War Tax on club dues \$15.45	101.45
13. Expenses in connection with Item 2 above (From Schedule A)	
14. Expenses in connection with Item 6 above (From schedule C)	
15. Exempt Income (Listed in Item 8 above).....	411,359.65
16. Other Deductions authorized by law (Explain) Commission on collection of income.....	1,131.88
.....	
17. Total Deductions in Items 11 to 16 (Carry to Item 19 at Top)	<u>\$428,275.22</u>

COMPUTATION OF TAX

(Do Not Use)

18. Total Income	\$421,329.64	\$421,329.64
19. Deductions	428,275.22	21,705.24
deficit*		
20. Net Income	6,945.58*	319,624.40
21. Exemption	1,400.00	1,400.00

22. Taxable Income	none	318,224.40
23. Tax	\$ none	\$ 18,686.22
		<hr/>
1st Payment		9,343.11
(Delinquent after June 20)		
2nd Payment		9,343.11
(Delinquent after Nov. 15)		

*Denotes red letters and figures.

AFFIDAVIT

I swear (or affirm) that this return has been examined by me and, to the best of my knowledge and belief, is a true and complete return made in good faith.

HAWAIIAN TRUST CO., LTD.

By (Sgd.) H. W. CAMP

Signature of Taxpayer or Agent.

Asst. Secretary.

120 S. King St. Honolulu

Official Capacity and Address of Agent.

Subscribed and sworn before me this 18th day of June, A. D. 1931.

(Notarial Seal)

(Sgd.) H. J. EVENSEN

Deputy Assessor or Notary Public.

Notary Public First Judicial Circuit,

Territory of Hawaii.

SCHEDULE A—EXPENSES OF BUSINESS OR PROFESSION

Cost of Goods Sold:

1. Labor	\$.....
2. Materials and Supplies	
3. Merchandise bought for Sale	
4. Other Costs (List principal items).....	
5. Plus Inventory at first of year.....	
6. Total (Lines 1 to 5 inclusive).....	\$.....
7. Less Inventory at end of year.....	
8. Net Cost of Goods Sold	\$.....

State amount of salary, or its
equivalent, paid to self and
included in Line 9 hereof

\$.....

Other Deductions:

9. Salaries and Wages\$.....
(Not reported in Line 1 hereof)
10. Rent on Business Property
(Where taxpayer has no equity)
11. Insurance on Business Property
12. Depreciation on Business Property.....
(Actually in use)
13. Repairs to Business Property
(Explain below)
14. Bad Debts (Explain below)
15. Other expenses
(List principal items)
16. Total (Lines 9 to 15 inclusive).....\$.....
17. Total Deductions (Line 8 plus Line 16)
(Enter as Item 13)\$.....

Explanation of deductions claimed
(Lines 4, 13, 14 and 15)

.....

.....

.....

State estimated life of property and how depreciation
is arrived at (Line 12)

.....

SCHEDULE B—PROFIT FROM REDEMPTION OF REAL ESTATE, STOCKS, BONDS, ETC.

Kind of Property	Date Acquired	Date Redeemed	Redemption Price	Commis-sions	Cost Price	REAL ESTATE			Net Profit (Enter as Item 5)
						Value 5 Years Prior to Sale	Subsequent Improvements	Total	

600 shs	1926	1930	\$	\$	\$60,000.00	\$	\$	\$	none
---------	------	------	----	----	-------------	----	----	----	------

E. J. Lord Ltd.

State how 5-year value is determined

SCHEDULE C—EXPENSES OF RENTED PROPERTY

Kind of Property	Commis-sions	Deprecia-tion	Repairs	Insurance	Water, Light, Etc.	Other Expenses (Enter as Item 14)	Total (Enter as Item 14)
------------------	--------------	---------------	---------	-----------	--------------------	-----------------------------------	--------------------------

State estimated life of property and how depreciation is arrived at

Explain nature of repairs

The New Freedom Press
Com. on Pub. Accy. Form B22.

CORRECTED.

Territory of Hawaii

First Taxation Division Honolulu, T. H. June 19, 1931.

E. J. Lord

c/o Hawaiian Trust Co., Ltd. Honolulu, T. H.

NOTICE OF PROPOSED CHANGE IN ASSESSMENT ON INCOME TAX RETURN

Please be advised that certain items in your income tax return for this year are not in conformity with the law. The following summary shows the amounts returned by you and the corrected amounts as changed by the Assessor.

	AS RETURNED	AS CHANGED
Gross Income	\$527,598.20	\$421,329.64
Deductions	534,543.78	21,705.24
Exemptions	1,400.00	1,400.00
Net Taxable Income	None.	398,224.40
Tax		18,686.22

Corrections are due to Sale of Stock as per schedule submitted.
Unless you can satisfy the Assessor that the figures returned by you are correct, the amended figures will stand as proposed herein.

(Sgd.) CHAS. CHING QUON
Dep. Assessor.

Delivered by H. Glass to Mr. Carter Galt.
6/19/31 (Sgd.) H. GLASS

Territory of Hawaii

9

Received
6/18/31
(s) H. Glass

June 17, 1931

E. J. LORD

1930 Territorial Income Tax

Schedule showing basis of Income Tax Assessor's figure and
adjustment thereto to agree with amended return.

Date of Payment		Assessor's Figure
	Proceeds from redemption of 600 shs E. J. Lord Ltd	<u>\$476,074.00</u>
Feb 15 1930	Notes and Bonds \$249,000.00	
	Cash 1,000.00	
Jul 16 1930	Bonds, St. Louis Heights 23,000.00	
	Cash 373.00	
	Accrued interest on bonds 482.36	
	St. Louis Heights, 2/15/30 to 7/16/30	273,855.36
Dec 26 1930	Bonds 107,000.00	
	Cash 67,036.12	
(a)	Interest on above \$67,036.12 cash item from July 31 to Dec 31 1930 at 2% monthly	670.36
(b)	Accrued interest on bonds 607.50	
	St. Louis Hts	
	1/2 mo \$141.67	
	Ark Power & Light	
	2 mo 91.66	
	Alabama Power	
	4 mo 166.67	
	Texas Power & Lt	
	3 mo 125.00	
	Emporium Capwell	
	Corpn 2 mos 82.50	
	<u>\$607.50</u>	175,313.98

Payable

in 1931 (c) Proportion of E J Lord's
1930 estimated federal
income tax assumed
and payable by E J
Lord Ltd in 1931

26,904.66

Total proceeds, per
Assessor

\$476,074.00

LESS Cost

60,000.00

Balance subject to
tax, per assessor

\$416,074.00

Adjustments

The following items should be
deducted:

(a) Interest on \$67,036.12 670.36

This interest was not part
of the redemption transac-
tion and was therefore in-
cluded on taxpayer's orig-
inal return as part of item
#3—\$9969.99

(b) Accrued interest on bonds 607.50

This interest was not part
of the redemption transac-
tion and was therefore in-
cluded on taxpayer's orig-
inal return as part of item
#3—\$9969.99

[Seal]

[2]

(c) Reduction in amount of Federal 6,576.16

Income Tax liability assumed

by E J Lord Ltd

Federal tax as originally
computed \$26,904.66

Federal tax as
amended 20,328.50

\$ 6,576.16

Legal expenses paid by E J Lord	1,650.00	
not included in assessor's computation	<u>\$ 9,504.02</u>	\$ 9,504.02

NET AMOUNT ACTUALLY RECEIVED BY

E. J. Lord for redemption of 600 shares of
E J Lord Ltd stock over and above the cost
of said stock

Note: The taxpayer contends that this amount represents a distribution of earnings which have already been subjected to the Territorial income tax in the hands of the corporation and that such distribution is therefore specifically exempted from tax in the hands of the taxpayer, under the Territorial Income Tax Law.

[Seal]

[3]

INCOME TAX APPEAL.

[Endorsed]: Received June 30/31, Territorial Board of Equalization.

To—Harold C. Hill, Esq.,

Assessor of Taxes,

First Division, Territory of Hawaii.

APPEAL FROM ASSESSMENT.

You are hereby notified that the undersigned, having made a return showing the gross income received from all sources during the year immediately preceding the first day of January, 1931, the amount

of deductions therefrom and the amount of taxable income for such period; and having received notice that an assessment has been made in which the amount of taxable income has been raised above the amount in said return, as follows:—

	Returned	Assessed
Gross Amount of Income.....	\$527,598.20	\$421,329.64
Deductions	534,543.78	21,705.24
Amount of Taxable Income	None	398,224.40
Tax as graduated.....		18,686.22
Totals.....		\$ 18,686.22

And deeming himself aggrieved by the changes made in the amount of taxable income whereby the amount of taxes payable by the undersigned is increased from nothing, the amount payable according to such return, to \$18,686.22, hereby appeals from such assessment to the Territorial Board of Equalization, Territory of Hawaii, basing such appeal upon the following grounds:

1.

That the assessor of the First Taxation Division failed to give the tax payer notice of his raise in the amount of taxable income above the amount stated in the return of the tax payer within the time required by law to wit, R. L. H. 1925 Sections 1348 and 1396, said assessor having failed to give the tax payer notice of such raise prior to April 25, 1931.

2.

That the tax assessor erred in computing the gross income [4] of the tax payer for the year ending December 31, 1930.

3.

That the said tax assessor erred in computing the net income of the tax payer for the year ending December 31, 1930.

4.

That the said assessor erred in computing the amount of taxable income of the tax payer for the year ending December 31, 1930.

5.

That the said assessor erred in including in the income of the tax payer and refusing to allow as a deduction the amount received by the tax payer from E. J. Lord, Ltd., an Hawaiian corporation, the sum of \$406,569.98 as dividends upon the stock of such corporation upon the net profits of which said corporation a tax of 2% had been assessed, as required by R. L. H. 1925, Chapter 103.

Dated at Honolulu, T. H. June 18, 1931.

(Sgd.) E. C. PETERS

Attorney for tax payer—E. J. Lord. [5]

Before the Territorial Board of Equalization, Territory of Hawaii, Honolulu, Hawaii.

In the matter of the Income Tax Appeal of

EDMUND J. LORD

For the year ending December 31, 1930,
First Taxation Division.

DECISION.

The Taxpayer, Edmund J. Lord, filed with the Tax Assessor, First Division, his individual income tax return for the twelve months preceding January 1, 1931, in which he claimed a deficit of \$6,945.58 and an exemption of \$1,400.00, a total deficit and exemption of \$8,345.58.

The Tax Assessor disallowed a deduction claimed by the Taxpayer amounting to \$406,569.98 and found the Taxpayer's net taxable income to be \$398,224.40 on which he imposed an income tax amounting to \$18,686.22, whereupon the Taxpayer appealed to this Board.

Prior to 1930 the Taxpayer owned 600 of the 1000 shares of stock of E. J. Lord, Ltd., and during the year 1930 delivered his stock to that Company. Before this Board the Taxpayer contended that the difference between the total amount he received from E. J. Lord, Ltd., for his 600 shares of stock and the amount of his original investment of \$60,000.00 for this stock, was a dividend, a distribution to him of 60% of the accumulated earnings or surplus of the Company; that since the net earnings

of the Company had been each year properly shown on the Company's Territorial Income Tax Return and income taxes had been levied thereon by the Tax Assessor and paid by the Company, these earnings should not again be subjected to income tax when distributed to stockholders; that, in effect, this transaction with the Company was [7] a sale and a delivery by him to the Company of his 600 shares of stock for \$60,000.00 and a dividend paid to him by the Company.

The Tax Assessor's contention was that no dividend was declared or paid in 1930 other than a dividend of \$25,000.00 regularly entered in the Company's books of record,—in which, it developed, the Taxpayer did not participate since he had delivered his stock to the company prior to the date of the declaration of this dividend of \$25,000.00,—and that the transaction was purely a sale of the Taxpayer's 6000 shares of stock to E. J. Lord, Ltd., at a price for the whole 600 shares, and that the difference between what the Taxpayer paid for the 600 shares and what he received from the Company for the transaction, upon the relinquishment of these shares by him to the Company, was taxable income upon which the Tax Assessor had properly levied an income tax.

This Board is of the opinion that the records of the Company show conclusively that the Company intended the transaction to be wholly a sale, as for example;—

(1) In the minutes of a special meeting of the Board of Directors of E. J. Lord, Ltd., held on

December 7, 1929, (Taxpayer's Exhibit 30a) the manner of the proposed purchase by the Company of the Taxpayer's 600 shares of stock is recorded with a specific provision that the Company should pay the Taxpayer 40% of the amount to which Mr. E. J. Lord may become liable for Federal and Territorial Income taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares'';

(2) In an agreement entered into between the Taxpayer and E. J. Lord, Ltd., on December 13, 1929, (Taxpayer's Exhibit 9) the manner of payment by the Company for the sale to it of the Taxpayer's 600 shares of stock in the Company is set forth in detail and one of the provisions of the agreement is that 40% of the amount of Federal and Territorial Income Tax upon income accruing and to accrue to the Taxpayer by reason of the "consummation [8] of the sale of said 600 shares "shall be paid by the Company to the Taxpayer "forthwith upon assessment'';

(3) In the minutes of a meeting of the Board of Directors of E. E. Black, Ltd.,—successor to E. J. Lord, Ltd.,—held on December 20, 1930, (Taxpayer's Exhibit 38c) reference is again made to the agreement of the Company to pay 40% of the said taxes;

(4) In Taxpayer's Federal Income Tax return for the calendar year 1930, (Tax Assessor's Exhibit A) in Schedule D thereof, the disposition of the said 600 shares of stock is listed as a sale of capital

assets to E. J. Lord, Ltd., and a tax of $12\frac{1}{2}\%$ was imposed on the gain;

(5) In the Annual Corporation Exhibit of E. E. Black, Ltd., for the year ending December 31, 1930, (Taxpayer's Exhibit 6f) "Treasury stock" is listed among the assets. There is no such item listed among the assets in the comparative list of assets for 1929 of the same Corporation Exhibit. No other stock than Taxpayer's 600 shares was purchased by the Company in 1930.

In a hearing before this Board on Monday, December 7, 1931, (page 117 of the transcript) E. E. Black testified that it was the intention of E. J. Lord, Ltd., to redeem the capital stock held by the Taxpayer "because it was representing my ambition of a life-time to own my own company".

In arguing the case before this Board, counsel for E. E. Black (pages 202-203 of the transcript) contended that there was a distribution to E. J. Lord of 60%, his interest in the profits of the corporation and his original contribution of capital; that, inasmuch as E. E. Black was left in the corporation and owning every share of the corporation, this was a distribution, that the transaction "was a distribution between Johnny Black on the one hand and Mr. Lord on the other". [9]

This Board disagrees with the above contention. The Board holds that on December 31, 1930, E. E. Black, Ltd., and not E. E. Black was the owner of the 600 shares purchased from the Taxpayer; that E. E. Black's ownership of stock was limited

to 40%—less the two or three shares nominally held by the other directors—and that there had been no distribution to E. E. Black.

The Taxpayer cannot be permitted to come in now and maintain the claim that the transaction was a dividend, a distribution of surplus upon which no further Territorial Income Tax should be paid, while the records of the Company fail to show that E. E. Black the 40% stockholder, received as an individual any portion of the distribution. The records do show that a sale was intended and was consummated.

In cross-examination before this Board of H. Glass, head of the Territorial Income Tax Bureau, counsel for E. E. Black (page 166 of the transcript) contended that no Territorial Income tax would have accrued had the Company taken what he called “the long way round, the red-tape proposition” of declaring and paying a dividend to both the Taxpayer and E. E. Black, but he failed to state the very obvious fact that had the Company so acted, both the Taxpayer and E. E. Black would have received dividends of such large amounts that the sum of their Federal surtaxes accruing on the same would have greatly exceeded the amount of the Federal Tax actually paid by the Taxpayer on his gain on the sale of capital assets, plus the amount of the Territorial Income tax levied in 1931 against the Taxpayer.

This Board finds for the Tax Assessor and hereby decides that the Taxpayer had for the twelve months

preceding January 1, 1931 a taxable income of \$398,224.40, on which a territorial income tax amounting to \$18,686.22 shall be paid. [10]

TERRITORIAL BOARD OF EQUALIZATION

(Sgd.) CHAS. T. WILDER

Chairman,

(Sgd.) JOHN J. WALSH

Member,

(Sgd.) ANDREW ADAMS

Member.

Honolulu, Hawaii.

January 20, 1932. [11]

[Title of Court and Cause.]

APPEAL AND NOTICE OF APPEAL.

Comes now, Edmund J. Lord, the taxpayer in the above entitled matter, and hereby gives notice of appeal and does hereby appeal to the Supreme Court of the Territory of Hawaii from the decision of the Territorial Board of Equalization, Territory of Hawaii, made and entered in the above entitled matter on the 20th day of January, 1932, finding for the Tax Assessor, First Division, Territory of Hawaii, and against the Taxpayer and deciding that said taxpayer had for the twelve months preceding January 1, 1931 a taxable income of \$398,224.40 on which the Territorial income tax amounted to \$18,286.22 shall be paid; and said taxpayer prays that all of the records in said matter, together with

the reporter's transcript of evidence, all exhibits and all other evidence, and this Notice of Appeal and Appeal, be forwarded to the Clerk of the Supreme Court of the Territory of Hawaii.

Dated: Honolulu, Territory of Hawaii, this 29th day of January, 1932.

EDMUND J. LORD

By PROSSER, ANDERSON,
MARX & WRENN

His Attorneys.

By (Sgd.) HEATON L. WRENN

The service of a copy of the
within

Appeal & Notice of Appeal
this day admitted

Dated Jan. 30

(Sgd.) H. T. KAY

Attorney for Assessor [13]

[Endorsed]: Filed February 1, 1932, at 11:40
o'clock a. m. (Sgd.) Robert Parker, Jr., Clerk
Supreme Court. [12]

[Title of Court and Cause.]

CERTIFICATE.

I hereby certify that the above entitled matter was heard before this Board on the Taxpayer's appeal from the assessment of the Tax Assessor, First Division, and that the Taxpayer now appeals to the Supreme Court of the Territory of Hawaii

from the decision of this Board finding for the Tax Assessor; that

- (1) Net taxable income found by the Assessor, \$398,224.40 and tax thereon \$18,686.22;
- (2) Net taxable income returned by Taxpayer, none and tax thereon none;
- (3) Net taxable income fixed by this Board, \$398,224.40 and tax thereon \$18,686.22;
- (5) Points of law, none.

I further certify that the following constitute all of the records before this Board in the above case and submit same herewith:—Taxpayer's return, Notice of Assessment by Assessor, Decision of this Board, 238 pages of the transcript of evidence, Exhibits "A to E-3" inclusive of the Assessor, Exhibits "1 to 38-c" of the Taxpayer, Appeal and Notice of Appeal together with Statutory costs in the amount of \$1,106.56 and letter from Messrs. Prosser, Anderson, Marx and Wrenn, Attorneys for Taxpayer protesting the payment to this Board of the Statutory costs.

Witness my hand this first day of February 1932.

(Signed) CHAS. T. WILDER

Chairman,
Territorial Board of Equalization,
Territory of Hawaii. [14]

No. 2052.

In the Supreme Court of the Territory of Hawaii.

October Term, 1933.

Appeal from Territorial Board of Equalization.

In the Matter of the Income Tax Appeal
of

EDMUND J. LORD,

For the year ending December 31, 1930,
First Taxation Division.

OPINION OF THE COURT.

[Endorsed]: Filed Dec. 2, 1933 at 9:40 o'clock
a. m. (Sgd.) Robert Parker, Jr., Clerk Supreme
Court. [15]

Argued October 26, 1933.

Decided December 2, 1933.

PERRY, C. J., BANKS AND PARSONS, JJ.

Taxation—income tax—profits from sale of movable property.

When all of the stock of a corporation is held by two persons and one of the stockholders sells to the corporation and the corporation repurchases from him all of his stock for an agreed consideration larger than the amount originally contributed by the seller for the stock, the resulting gain to the stockholder is taxable as income, even though a part of the consideration paid by the corporation was derived from undistributed profits upon which it had already paid an income tax of two per cent.

Upon the facts and evidence recited in the opinion, *held*, that the transaction between one of two sole stockholders and the corporation was a sale by him and a repurchase by it and was not and did not include a payment in the nature of a dividend by the corporation to the stockholder. [16]

Same—same—taxation period—time of accrual of profits.

Under sections 1388 and 1391, R. L. 1925, the profits resulting to a stockholder from the sale of his stock are taxable as income of the year during which the sale was made irrespective of whether or to what extent the increase in value in reality accrued during preceding years.

Same—profits from sale—dividends—intention of parties.

In determining whether a transaction relating to the transfer of all of his stock by the holder thereof to the corporation and the acquisition of the same by the corporation was a sale by the stockholder and a repurchase by the corporation or was, in part at least, the payment of a dividend out of undistributed profits which had already borne an income tax of two per cent, the question is one largely of the intention of the parties who took part in the transaction. [17]

OPINION OF THE COURT BY PERRY, C. J.

This is an appeal from the decision of the board of equalization sustaining an assessment against E. J. Lord, the appellant, of an income tax upon certain moneys received by him during the year preceding January 1, 1931.

E. J. Lord and E. E. Black, having been prior thereto associated in the contracting and building business, in September, 1926, formed a corporation under the name of E. J. Lord, Limited. The corporation had a capital stock of \$100,000 in one thousand shares, six hundred shares of which were issued to E. J. Lord and four hundred shares to E. E. Black, Lord contributing in payment of the stock money or other capital of the value of \$60,000 and Black contributing money or other capital of the value of \$40,000. Apparently to comply with the requirements of the law relating to the formation of corporations, three other stockholders were named, each as the holder of one share, but, as testified to by Black at the trial before the board, these three held the shares only "nominally" and were in reality "dummies." In each of the annual reports subsequently filed with the treasurer of the Territory only two persons were named as holders of the capital stock and these were E. J. Lord as holding six hundred shares and E. E. Black as holding four hundred shares.

The corporation met with a large measure of success and received substantial profits from its operations.

Late in 1929 E. E. Black, whose ambition had long been to form and control a corporation of his own, and E. J. Lord, who, because of ill health and perhaps for other reasons, desired to retire from the active pursuit of that business, after various discussions came to the understanding that Lord would retire and [18] that Black would continue the business. On December 13 of that year they signed a written document which had been prepared by learned counsel, a former chief justice of this court, stating the terms of the understanding which the two had so reached. There was included in the agreement the grant to E. J. Lord Company, Limited, of an option to acquire the six hundred shares owned by E. J. Lord, for a consideration therein stated. Shortly thereafter the option was accepted by the corporation and in due course, in part early in 1930 and in part in December of 1930, the sum of \$468,219.98 was paid to Lord in accordance with the terms of the contract.

Subsequent to the acceptance of the option the name of the corporation was changed to E. E. Black, Limited, and its capital stock was reduced to \$40,000 divided into four hundred shares, all of which was held by E. E. Black. Section 1391, R. L. 1925, which is part of chapter 103, relating to income taxes, provides that "in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corpora-

tion if the tax of two per centum has been assessed upon the net profits of such corporation as required by this chapter." It is undisputed that the money paid to E. J. Lord under the contract referred to, other than the sum of \$60,000 which came from capital, was actually paid by the corporation out of undivided profits, partly earned prior to the date of the contract and partly earned after the date of the contract and that upon all of these undivided profits the corporation had paid the tax of two per cent required by law. The contention of the taxpayer-appellant is that the moneys received by him in 1930 (other than \$60,000 thereof) were received by him "as a dividend" out of profits which had already borne the statutory tax of two [19] per cent and are, therefore, exempt from taxes as income of E. J. Lord. The contention of the Territory, on the other hand, is that in the transaction between Lord and Black there was not any payment of a dividend and that there was simply a sale by Lord and a purchase by the corporation of the six hundred shares of the capital stock owned by Lord and a payment therefor of the purchase price in which was not involved or included any idea of a dividend. A second claim by the appellant is that even if the moneys in question were not received by Lord "as a dividend" but are to be deemed gains or profits derived from the sale of personal property, still no tax is assessable thereon because the increase in value of the six hundred shares over and above \$60,000 accrued during the years 1926,

1927; 1928 and 1929 and did not accrue wholly during the taxation year of 1929.

The main question is, what was the nature of the transaction between the corporation and Lord? As to the \$60,000 there is no dispute. It was a restoration to Lord of the capital which he had contributed. As to the remainder, was it received by Lord as a dividend? The board of directors of E. J. Lord, Limited, held a meeting on December 7, 1929, to consider the proposal then pending. Under the title of "Purchase of Stock" the minutes of that meeting say: "Mr. E. E. Black moved that as Mr. E. J. Lord was willing to sell all his stock of E. J. Lord, Ltd., the company was to redeem the 600 shares for which the company was to pay for the said shares in the following manner: (1) The sum of money equal to 60% of the net worth of the company as of December 31st, 1929; (2) the sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929; (3) the sum of money equal to 40% of the amount to which Mr. E. J. Lord may become liable for federal and territorial income taxes upon [20] income accrued and to accrue to him resulting from the sale of said 600 shares. Mr. Lord agreed to give the company an option to purchase the above mentioned stock to February 28th, 1930, and to have an agreement drawn signed by both parties covering the above option, price and payments to be made, a copy of such agreement to be entered into the minute book." This motion

carried unanimously. Another motion adopted at the same meeting was: "That the company upon the exercise of the option cause its articles of association to be amended" so as to effectuate a change of name.

Then followed the carefully drawn agreement of December 13, 1929, which was intended as appears from the evidence, to be a written record of what the agreements were. Omitting irrelevant portions, that instrument recited and declared, referring to E. J. Lord's six hundred shares of capital stock, that the corporation "desires to redeem said shares of stock;" that Lord "is willing to accept as consideration for the sale of said stock" to the corporation and the corporation "is willing to pay" to Lord "for the redemption of said stock, a sum of money equal to sixty per cent (60%) of the net worth" of the corporation "as of December 31, 1929, and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue" to the corporation "by its completion of the respective works contemplated by certain executory contracts to which" the corporation "is a party, remaining uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which" Lord "may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and/or to accrue to him by reason of and resulting from the exercise" by the corporation "of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock" of the corpora-

tion; that "the net worth of the" corporation "cannot be [21] determined until the books" of the corporation "have been closed for the year 1929 and an audit made thereof;" that certain enumerated contracts were uncompleted; that therefore Lord "does hereby * * * " (a) "give and grant" to the corporation "an option, irrevocable within the time for acceptance herein limited, to purchase free from encumbrances the said six hundred (600) shares of the capital stock" of the corporation "so owned by him * * * for the consideration hereinafter set forth," (b) "assign and deliver" to the corporation the same six hundred shares, duly endorsed, "by way of pledge to secure the performance" of Lord's covenants and (c) appoint the corporation his attorney "upon the exercise of the option hereby granted" to cause the said six hundred shares "of the capital stock * * * to be redeemed" by the corporation and "to be recorded on the proper books" of the corporation. The corporation, on the other hand, agreed (1) to close its books as of December 31, 1929, and to have them audited, (2) to faithfully complete the uncompleted contracts in as economical manner as possible, (3) to have its books open to the inspection of Lord at all times and (4) that "upon the exercise of the option by it to it hereby granted," it will, "as soon as may be, cause its articles of association to be amended" so as to effectuate the desired change of name. Both parties mutually covenanted and agreed therein (1) that "the option

hereby given shall be open for acceptance up to, but not after the 28th day of February, 1930," (2) that "the purchase price of the said stock" should be, reciting the precise language earlier in the document used, "a sum of money equal to sixty per cent (60%) of the net worth" of the corporation as of December 31, 1929, "a sum of money equal to sixty per cent (60%) of the net profits yet to accrue" to the corporation "by its completion" of the uncompleted contracts and "the further sum of money equal to forty per cent [22] (40%) of the amount" which Lord "may become liable" to pay "for income taxes upon income accrued and to accrue to him by reason of and resulting from the exercise" by the corporation "of the option hereby granted and the consummation of the sale" of the six hundred shares. The document further recites "that such purchase price shall be paid" to Lord as follows: "The sum of money equal to sixty per cent (60%) of the net worth" of the corporation "as of December 31, 1929, forthwith upon the exercise" by the corporation "of the option hereby granted to it. In the event that the amount so payable exceeds the sum of two hundred fifty thousand dollars (\$250,000.00), the amount of the excess over that sum may be retained" by the corporation "until and paid by it to" Lord "upon the completion of the St. Louis Heights contract and the receipt by it of the full consideration for the performance thereof, the sum of money equal to sixty per cent (60%) of the net profits yet to accrue from each of the foregoing enumerated uncompleted contracts

when completed and the moneys, bonds or other consideration accrued and payable or deliverable" to the corporation "thereunder, reduced to possession, and the sum of money equal to forty per cent (40%) of the income tax" which Lord might become liable to pay "for income taxes upon income accrued or to accrue to him by reason of and resulting from the exercise by" the corporation "of the option hereby granted and the consummation of the sale" of the six hundred shares "forthwith upon assessment."

Under date of February 15, 1930, Lord signed a paper whereby he acknowledged receipt of the sum of \$250,000 in money or its equivalent, from the corporation, which paper read as follows: "E. J. Lord, Limited having duly accepted the option granted by me to it by the indenture of agreement between us dated December 13, 1929, and the sum of two hundred seventy-three thousand eight [23] hundred fifty-five dollars and thirty-six cents (\$273,855.36) having been found to be sixty (60%) of the net worth of E. J. Lord, Limited, as of December 31, 1929; I hereby accept in lieu of cash and acknowledge receipt from E. J. Lord, Limited, in payment of the sum of two hundred fifty thousand dollars (\$250,000.00) on account of the purchase price of the six hundred (600) shares of the capital stock of E. J. Lord, Limited, the subject of said indenture, the following enumerated notes, bonds and cash,"—followed by an enumeration of the property transferred and received.

These are the formal documents which the parties executed as setting forth the terms of the transaction. Nowhere is there the slightest reference to a dividend declared, paid or received. Nowhere in the books of the corporation, as exhibited in evidence, is there any treatment of these payments to Lord or of any part thereof as a dividend or dividends. (The books do contain entries showing the payment of dividends during the four-year period.) The essence of the transaction, as disclosed by the minutes of the corporation, by the formal memorandum of contract, by the formal receipt and by the testimony, is that Lord sold to the corporation and that the corporation bought back (that is what the word "redeem" means) from him the six hundred shares of stock. There is nothing in the use of the word "redeem" or of the word "redemption" that indicates the making or the receiving of a dividend. It simply imports, as used in connection with these shares of capital stock, that the corporation which once issued or gave out the stock repurchased it or bought it back. Its use is entirely consistent with the statement in the same contract that Lord was *selling* the stock and does not in any wise qualify the use of the word "sale".

Counsel for the appellant urges that the ultimate result [24] to the parties would have been the same if the corporation had on one day declared and paid a dividend of sixty per cent of its undistributed profits and then on the next week or the next day bought Lord's six hundred shares for the sum of

\$60,000. That may be assumed to be a correct statement; but it does not affect the conclusion which ought to be reached in this case. It is not for us to consider now what the parties might have done. What is before us for consideration is, what did they actually do? This is necessarily, in large measure, a question of the intention of the parties. The instruments and records above recited are susceptible of only one interpretation in that respect and that is that the parties understood and intended that Lord was selling and that the corporation was buying the six hundred shares. Not only was there no reference to a dividend in the records evidencing the transaction but the statements made tend to exclude and to render impossible the thought of a dividend. The parties declared that it was a sale and a purchase; they declared that a part of the consideration should be a sum of money equal to sixty per cent of "the net worth of the corporation," which net worth must have necessarily included capital as well as the undistributed profits, and they did not, in that connection, distinguish between the two; that another part of the consideration was to be a sum of money equal to sixty per cent of the net profits to accrue in the future from contracts then uncompleted. They did not say that it should be sixty per cent of the net profits but did say that it should be a sum of money equal to sixty per cent of the net profits. Was the corporation on December 13, 1929, declaring a dividend out of profits not yet earned and which might not be earned for a

year longer? Moreover, in the transaction the corporation did not pay any money or deliver [25] any equivalent property to Black. He certainly did not receive any dividend. While it may be legally possible for one only of two shareholders to receive a dividend the other consenting to defer his dividend to a later time, that arrangement, when claimed to exist, should at least be shown by clear and convincing evidence; and in the case at bar there is no evidence whatever of any such arrangement. A dividend could as well have been paid to Black and the money by him later reinvested in his corporation but that is not the course that was followed.

Another consideration, not controlling and yet relevant, is that the exemption provided for in the provisions of section 1391, above quoted, is that in favor of amounts received from a corporation "as dividends *upon the stock*"* of that corporation. This would seem to presuppose the payment of a dividend to one who holds stock rather than to one who by the very transaction is relinquishing the stock to the corporation. If the legal possibility of one who is relinquishing stock in the same transaction receiving a dividend upon that stock is not excluded, at least it would require some evidence on the part of the parties to the transaction to indicate that some or all of the moneys paid to the out going stockholder were being paid as a dividend. There are no such indications in the case at bar.

*Italics by the Court.

The conclusion is irresistible that irrespective of what the parties might have accomplished if they had pursued a different course, the transaction as it actually occurred was a sale and purchase and resulted in a profit to Lord in the sale of his stock.

The other contention of appellant likewise cannot be sustained. Section 1388, R. L. 1925, provides that "there shall be levied, assessed, collected and paid annually upon the gains, profits and income received by every individual residing in the Territory, from all property owned, * * * a tax in accordance with the follow- [26] ing schedule on the amount so received during the taxation period." The schedule of rates of taxation follows. Section 1390 provides that "in estimating the gains, profits and income of any person or corporation, there shall be included * * * the amount of sales of all movable property, less the amount expended in the purchase or production of the same * * * and all other gains, profits and income derived from any source whatsoever during said taxation period." In the face of this language of the statute, the contention that the profits resulting from the sale of stock were not taxable in January, 1931, because they did not wholly accrue during the year 1930, is untenable. The requirement of the statute was that in January, 1931, liability would accrue for taxes on income which was "received" or "derived" during the taxation period, which was the year 1930; and this is made even more clear with reference to the sales of movable property when the statute de-

clares that in estimating the profits “there shall be included * * * the amount of * * * less the amount expended in the purchase.” The legislature did not, in this connection, make any exception of those parts of the gain in value which did not accrue during the taxation year and the court cannot now make the exception.

Reliance is had by the appellant upon the case of *Gray v. Darlington*, 15 Wall. 63, 65. That case was decided upon the federal statute of 1867, which taxed certain classes of income “*for** the year” preceding the taxation date. Income or gains or profits “for” a stated year can well be held to exclude gains or profits accruing during other years. This distinction was pointed out by the same court in *Hays v. Gauley Mt. Coal Co.*, 247 U. S. 189, 191, 192. The latter case was decided under the Act of 1909, which taxed “the entire net income * * * received by it” (the taxpayer) “*during** [27] such year,” which is the equivalent of the expression used in our statute for the admeasurement of taxable income. It was held in the *Hays* case that the Act of 1909 “measured the tax by the income received within the year for which the assessment was levied, whether it accrued within that year or in some preceding year while the Act was in effect,”—with an exception not material to the case at bar. And see *Ewa Plantation v. Wilder*, 26 Haw. 299, in which it was held that a sum received by the

*Italics by the Court.

taxpayer in liquidation of losses or damage sustained in consequence of a laborers' strike is to be regarded as income of the year in which it is received and may not be attributed to the years in which the damaged crops of cane were sold.

The decision of the board of equalization is affirmed.

(Sgd.) ANTONIO PERRY.

(Sgd.) JAS. J. BANKS.

(Sgd.) CHARLES F. PARSONS.

H. L. Wrenn (Prosser, Anderson,
Marx & Wrenn on the briefs) for
taxpayer.

E. C. Peters for E. E. Black, Ltd.

H. T. Kay, First Deputy Attorney Gen-
eral, for the assessor. [28]

[Title of Court and Cause.]

JUDGMENT.

[Endorsed]: Filed Jan 25, 1934 at 2:45 o'clock
p. m. (Sgd.) Robert Parker, Jr., Clerk Supreme
Court. [29]

The above entitled cause having been argued on
the 26th day of October, 1933, by H. L. Wrenn,
Esq., Attorney for the taxpayer, and having here-
tofore been submitted on briefs by E. C. Peters,
Esq., attorney for E. E. Black, Limited, and H. T.
Kay, Esq., First Deputy Attorney General, attorney
for the tax assessor, and the court having hereto-

fore on, to-wit, the 2nd day of December 1933, rendered its decision herein in favor of the tax assessor and against the taxpayer, now, therefore, pursuant to and in conformity with said decision,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the decision of the board of equalization is affirmed.

Dated at Honolulu, T. H., this 25th day of January 1934.

BY THE COURT:

(Sgd.) ROBERT PARKER, JR.,

[Seal]

Clerk.

Approved:

(Sgd.) ANTONIO PERRY,

Chief Justice.

O. K. as to form

Prosser, Anderson, Marx & Wrenn

E. C. Peters. [30]

[Endorsed] Filed February 1, 1932 at 11:40 o'clock a. m. Robert Parker, Jr., Clerk, Supreme Court.

Before the Territorial Board of Equalization
Territory of Hawaii.

[Title of Cause.]

TRANSCRIPT OF EVIDENCE.

The above entitled matter came duly on for hearing before the aforesaid Board on Friday, December 4, 1931, at 9:15 o'clock a. m., the Chairman,

the Honorable Charles T. Wilder, and the Honorable John J. Walsh, being present,

Harold T. Kay, Esq., Deputy Attorney General, appearing for the Tax Assessor, and

Heaton L. Wrenn, Esq., of the firm of Messrs. Prosser, Anderson, Marx and Wrenn, appearing for the Taxpayer, E. J. Lord, and

E. C. Peters, Esq., appearing for E. E. Black, Limited.

WHEREUPON the following proceedings were had and testimony taken:

Mr. KAY: Is the Board ready to go ahead?

M. WALSH: We are ready. We have a reporter to make a transcript.

Mr. WRENN: We have some preliminary matters. I see no reason we cannot go ahead.

Mr. KAY: Well, if the Board cares to go ahead at this time, I have no objection.

The CHAIRMAN: Mr. Adams can read the transcript afterwards. [31]

Mr. KAY: I have asked Mr. Nye to bring certain papers in regard to E. J. Lord, Limited, and E. E. Black, Limited. Have you the original articles of incorporation of E. J. Lord, Limited?

Mr. NYE: Yes.

Mr. WRENN: I offer in evidence at this time, on behalf of the taxpayer, the original articles of association of E. J. Lord, Limited, filed in the office of the Treasurer of the Territory of Hawaii on September 7, 1926.

Mr. KAY: May I see what you have?

Mr. WRENN: May the original articles of association and affidavit of incorporation attached thereto, and Exhibit "A," be admitted as one exhibit.

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 1.")*

Mr. WRENN: May the petition for the amendment of the articles of association, changing the name from E. J. Lord, Limited, to E. E. Black, Limited, dated February 15, 1930, together with the certificate of the presiding officer attached thereto, the allowance of amendment, which is likewise attached thereto in this file, and the certificate for filing with the Registrar of Public Conveyances with the Treasurer be admitted as Exhibit 2 for Taxpayer?

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 2.")*

Mr. WRENN: And may the application for reduction of [32] capital stock of E. E. Black, Limited, filed in the Treasurer's office March 12, 1931, the application being dated March 7, 1931, together with the certificate of the officers of E. E. Black, Limited, on the reduction of capital stock attached thereto, and Exhibit "A" attached to the application showing the resolution of the shareholders, which is likewise attached thereto,—

Mr. KAY: Is there a reduction of stock made in 1931?

*Omitted from printed record on stipulation by counsel.

Mr. WRENN: Yes.

Mr. KAY: We will have to object.

Mr. WALSH: What does the reduction in capital in 1931 have to do with that?

Mr. WRENN: It has a great deal to do. We will show that at the time the original transaction was entered into between Taxpayer and E. J. Lord, Limited, it was the intention of E. J. Lord, Limited, to redeem this stock, and when it was redeemed from Mr. Lord to apply for the reduction of the stock of the company and cancellation of the stock, and that was duly carried out. We will show that the final payment on the amount which was to be made to Mr. Lord was not made until December 31, 1930. Subsequently in 1931 there was an adjustment to E. E. Black, Limited, on account of Federal income taxes, and immediately thereafter E. E. Black, Limited, applied for a reduction of the capital stock, which [33] application was granted, so it is very important.

Mr. KAY: If that bears on the 1930 income, we will withdraw our objection. We have no intention to object to anything relating to the 1930 income.

Mr. WRENN: Together with the affidavit of the notice to the Treasurer and approval of the reduction of the stock by the Treasurer on March 31, 1931.

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 3.")

TAXPAYER'S EXHIBIT 3

APPLICATION FOR REDUCTION OF CAPITAL STOCK OF E. E. BLACK, LIMITED.

To: The Honorable E. S. Smith, Treasurer of the Territory of Hawaii:

E. E. Black, Limited, a Hawaiian corporation, with a capital stock of \$100,000. divided into 1,000 shares of the par value of \$100. each, desires to reduce its capital stock to \$40,000. divided into 400 shares of the par value of \$100. each by retiring 600 shares of the par value of \$100. each, and herewith presents a sworn certificate as required by law signed by the presiding officer and secretary of an Annual meeting of stockholders of said corporation held on the Seventh day of March, 1931, showing what action was taken in the premises at said meeting.

The said corporation prays that you publish in a suitable newspaper in Honolulu a notice of said certificate as required by law, and after the time allowed by law has elapsed that you allow said reduction of capital of said corporation and enter the same of record, and that you do approve the retirement and cancellation of 600 shares of the par value of \$100. each with an aggregate par value of \$60,000.

Dated at Honolulu, T. H., March 7th, 1931.

E. E. BLACK, LIMITED,

By (signed) E. E. BLACK

Presiding Officer of said meeting

[Seal]

By (signed) T. IKEJIRI

Secretary of said meeting.

No. 2052. Filed February 1, 1932 at 11:40 o'clock a. m. (s) Robert Parker, Jr., Clerk Supreme Court. [264]

CERTIFICATE ON REDUCTION OF CAPITAL
STOCK OF E. E. BLACK, LIMITED.

Territory of Hawaii

City and County of Honolulu.—ss.

E. E. BLACK and T. IKEJIRI respectively duly sworn on oath, depose and say:

That the said E. E. Black was the presiding officer and said T. IKEJIRI was the Secretary of an Annual meeting of stockholders of E. E. Black, Limited, a Hawaiian corporation, duly convened in Honolulu, City and County of Honolulu, Territory of Hawaii, on the 7th day of March, 1931, for the purpose of considering a reduction of the capital stock of said corporation;

That at the time of said meeting the capital stock of said corporation consisted of 1,000 shares of the par value of \$100. each and of the aggregate par value of \$100,000.;

That at said meeting there were present or represented by proxy owners and holders of 1,000 shares, being all of the issued capital stock of said corporation, of which 600 shares were held in the treasury of said corporation, and all of the shares present or represented at said meeting voted for and in favor of a resolution to reduce the capital stock of the Company from \$100,000, to \$40,000 by retiring 600 shares of the par value of \$100. each of said corporation now held in the treasury;

That attached hereto and marked Exhibit "A" and made a part hereof is a true and correct copy of the resolution duly adopted and passed at said

meeting by a vote of all of the shares of the capital stock of said corporation;

That at the time of said meeting the assets of said corporation had a book value of \$174,958.63 and the said corporation owed, exclusive of its liability to its stockholders, the sum of \$7,149.86, and that said corporation was not then and has not since become otherwise indebted in any [265] manner over and above half the amount of \$40,000. which will be the remaining capital stock of said corporation after the proposed reduction has been effected.

(Signed) E. E. BLACK

(Signed) T. IKEJIRI

Subscribed and sworn to before me this 12th day of March, 1931.

[Seal]

(Signed) H. EDMUNDSON

Notary Public, First Judicial Circuit,
Territory of Hawaii. [266]

EXHIBIT "A"

E. E. BLACK, LIMITED

—Reduction of Capital Stock—

"WHEREAS E. E. Black, Limited, has an authorized capital stock of \$100,000. divided into 1,000 shares of the par value of \$100. each and has purchased from one of its stockholders 600 of said shares of the par value of \$100. each of the aggregate par value of \$60,000. and has paid for the same and holds the same in its treasury and desires to retire said 600 shares and to reduce its capital stock accordingly to \$40,000. divided into 400 shares of the par value of \$100. each,

“THEREFORE BE IT RESOLVED that the authorized capital stock of E. E. Black, Limited, be reduced from \$100,000. divided into 1,000 shares of the par value of \$100. each to \$40,000. divided into 400 shares of the par value of \$100. each by retiring 600 shares of the par value of \$100. each now held in the treasury;

“That a sworn certificate signed by the presiding officer and secretary of this meeting be presented to the Treasurer of the Territory of Hawaii setting forth therein the action taken and certifying that at the time the vote on this resolution was taken the corporation was not and has not since become indebted in any manner over and above half of the amount of its remaining capital stock;

“AND BE IT FURTHER RESOLVED that when the said reduction of capital stock is effected as required by law, the Treasurer of this corporation do retire and cancel the said 600 shares of the par value of \$100. each of this corporation now held in the treasury.” [267]

OFFICE OF THE TREASURER,
TERRITORY OF HAWAII.

Notice of the Reduction of the Capital Stock of
E. E. BLACK, LIMITED.

Notice is hereby given the E. E. BLACK, LIMITED, a corporation organized and existing under and by virtue of the laws of the Territory of Hawaii, has pursuant to law in such cases made and provided, duly filed in the office of the Treasurer of the Territory of Hawaii a sworn certificate, as re-

quired by law, showing the reduction of the capital stock of said corporation from a total amount of \$100,000.00, divided into 1,000 shares of the par value of \$100.00 each, to a total amount of \$40,000.00, divided into 400 shares of the par value of \$100.00 each.

Notice is further given hereby to all stockholders and creditors of said corporation, and to all persons claiming to be stockholders or creditors of said corporation, or otherwise interested therein, that all protests and objections to such reduction of capital stock must be filed in the office of the Treasurer of the Territory of Hawaii before the expiration of thirty days from the 17th day of March, 1931, (the date of the first publication of this notice) to be entitled to consideration.

Dated at Honolulu, T. H., March 16, 1931.

(Signed) E. S. SMITH

Treasurer, Territory of Hawaii.

HONOLULU STAR-BULLETIN: Publish the above notice in your issues of March 17, 24, 31, April 7, 14, 1931. Send bill to E. E. BLACK, Ltd., Pohukaina St., Honolulu, T. H. File AFFIDAVIT OF PUBLICATION in Office of Territorial Treasurer immediately after last publication. [268]

Territory of Hawaii,
Island of Oahu.—ss.

Before me, the undersigned, a Notary Public, this day personally came NELSON G. PRINGLE, who

being first duly sworn, according to law, says that he is the bookkeeper of the HONOLULU STAR-BULLETIN, a newspaper published at Honolulu, Territory of Hawaii, daily, except Sundays and that the ordered publication of

NOTICE OF REDUCTION CAPITAL

STOCK E. E. BLACK LTD.

was published in said paper on the following dates:
—MARCH 17-24-31 APRIL 7-14-, A. D. 1931.—

(Sgd.) Nelson G. Pringle

HONOLULU STAR-BULLETIN.

Subscribed and sworn to before me this 15th day of April, A. D. 1931.

[Seal]

(Sgd.) WM. J. FORBES

Notary Public, in and for the First
Judicial Circuit, Oahu, Territory
of Hawaii. [269]

OFFICE OF THE TREASURER OF THE
TERRITORY OF HAWAII.

In the Matter of the Reduction of the Capital Stock
of E. E. BLACK, LIMITED.

ORDER APPROVING REDUCTION
OF CAPITAL STOCK.

WHEREAS, at an annual meeting of the stockholders of E. E. BLACK, LIMITED, a Hawaiian corporation, duly called and held in Honolulu, City and County of Honolulu, Territory of Hawaii, on the 7th day of March, 1931, at which meeting there were present or represented by proxy owners and holders of 1,000 shares, being all of the issued cap-

ital stock of said corporation, of which 600 shares were held in the Treasury of said corporation, it was unanimously voted by said stockholders to reduce the capital stock of said corporation from a total amount of \$100,000.00 divided into 1,000 shares of the par value of \$100.00 each, to a total amount of \$40,000.00, divided into 400 shares of the par value of \$100.00 each; and

WHEREAS, a sworn certificate, as required by law, was on the 12th day of March, A. D. 1931, presented to the undersigned, setting forth therein the action taken at said meeting, and certifying that at the time said vote was taken said corporation was not and has not since become indebted in any manner over and above half of the amount of its remaining capital stock; and

WHEREAS, notice of said certificate and of such reduction of capital stock was published in a suitable newspaper, to wit: The Honolulu Star-Bulletin, in Honolulu, City and County of Honolulu, Territory of Hawaii, on to wit: the 17th, 24th and 31st days of March and the 7th and 14th days of April, 1931; and

WHEREAS, thirty days have expired since the first publication of [270] said notice and no protest or objection to such reduction of capital stock has been filed with the undersigned by any person claiming to be a stockholder or creditor of said corporation or any other person; and

WHEREAS, the undersigned is satisfied that the vote so certified was truly taken, and that said

corporation was not at the time of filing said certificate indebted beyond the limit aforesaid, and that there is no objection to such reduction of capital stock; and

WHEREAS, the fee required by law in such cases has been paid by said corporation;

NOW, THEREFORE, IT IS HEREBY ORDERED that such reduction and decrease of capital stock be and the same is hereby approved and allowed and entered of record in this office and that such reduction and decrease shall stand effected as of the date of the original filing of said certificate, to wit: the 12th day of March, A. D. 1931.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of the Treasurer's Office, Territory of Hawaii, at Honolulu, T. H., this 29th day of May, A. D. 1931.

[Seal]

(Signed) E. S. SMITH

Treasurer, Territory of Hawaii.

Decrease of Capital \$25.

Recording 1,500 wds 7.50

\$32.50

(Signed) HENRY A. NYE

Registrar of Public Accounts. [271]

Territory of Hawaii

Honolulu, Oahu.

OFFICE OF THE TREASURER.

I, E. S. SMITH, Treasurer of the Territory of Hawaii, do hereby certify that the foregoing is a true and correct copy of the Reduction of Capital

Stock of E. E. BLACK, LIMITED, reducing its capital from \$100,000.00 to \$40,000., by dividing into 400 shares of the par value of \$100. each, as on record in this office.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of the Treasurer's Office, Territory of Hawaii, at Honolulu, T. H., this 30th day of January, A. D. 1932.

[Seal]

(Signed) E. S. SMITH

Treasurer, Territory of Hawaii. [272]

Mr. WRENN: We offer in evidence as Exhibit 4 a record of the Treasurer's office showing the date of articles of incorporation September 3, 1926, (Sept. 7),

date of incorporation October 27, 1926, of E. J. Lord, Limited, and showing a capital stock of one hundred thousand dollars, filing number 1831.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 4.")*

Mr. WRENN: We would like to substitute this later on with copies,—and further record of E. E.

(12)

Black, Limited, showing that on March 1, 1931, its capital was forty thousand dollars.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 5.")

*Omitted from printed record on stipulation by counsel.

TAXPAYER'S EXHIBIT 5

Advertiser 166848 Recorded		Date of Charter Or Articles	Date of Incorporation	Date of Dissolution	Existence Years	Limit of Capital		Present Capital											
Book No.	Folio					Date	Amount	Date	No. Shares	Par Value	Amount								
37	78																		
43	189	Sept. 3, 1926	Sept. 7, 1926		50	Sept. 3 1926	1,000.00	Sept. 3, 1926	1,000	100.	100,000								
				(50			Mar. 12 1931	400	100	40,000								
				(2/24/30															
Officers																			
Date	Name	Title	Service of Process on																
		President																	
		Vice-President																	
		Secretary																	
		Treasurer																	
		Auditor																	
Annual Exhibits																			
Years and Filing Numbers																			
1911	1912	1913	1914	1915	1916	1917	1918	1919	1920	1921	1922	1923	1924	1925	1926	1927	1928	1929	1930
															83	25	49	32	65
Years and Filing Numbers																			
1931	1932	1933	1934	1935	1936	1937	1938	1939	1940	1941	1942	1943	1944	1945	1946	1947	1948	1949	1950
Nature of Business																			
Place of Principal Office																			
Honolulu																			
Name																			
E. E. BLACK LIMITED																			
Filing No.																			
1831																			

Formerly E. J. Lord Limited, name changed Feb'y 24, 1930
to

[Endorsed]: No. 2052. Filed February 1, 1932 at
11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court.

[273]

Mr. WRENN: I would like to offer as one exhibit at this time Exhibit 6, the annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1926.

(Document offered in evidence received [34] and marked: "Taxpayers' Exhibit 6A.")*

Mr. WRENN: The annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1927.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6B.")*

Mr. WRENN: The corrected annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1927.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6C.")*

Mr. WRENN: The annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1928.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6D.")*

Mr. WRENN: The annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1929.

(Document offered in evidence received and marked "Taxpayers' Exhibit 6E.")*

Mr. WRENN: And annual corporation exhibit of E. E. Black, Limited, for the year ending December 31, 1930.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6F.")*

*Omitted from printed record on stipulation by counsel.

Mr. WRENN: May we leave these until the conclusion of the case with the privilege of withdrawing them?

Mr. NYE: We will have to have them back.

Mr. WRENN: We will substitute copies.

Mr. KAY: May it please the Board, unless stipulated to by counsel that Mr. Adams may later consider this case by reading the evidence appearing in the transcript, it is going to be difficult for us to proceed. I suggest we wait until Mr. Adams appears. It is hardly proper for this Board to proceed and hear this evidence in the absence of one of the members. It would be hardly proper for the member to later consider the case, not hearing all the evidence.

Mr. WRENN: We are perfectly willing to stipulate that Mr. Adams can read the transcript and go ahead as if he were here. We will raise no objection to the fact that he is not here.

E. C. PETERS

was duly called and sworn as a witness for the Taxpayer, and testified as follows:

Direct Examination by Hearon L. Wrenn, Esq.

Q. Will you state your name, please?

A. E. C. Peters.

Q. Judge Peters, you are a member of the bar of all the Courts of the Territory of Hawaii?

A. Yes.

(Testimony of E. C. Peters.)

Q. And former Chief Justice of the Supreme Court of the Territory of Hawaii?

A. I was.

Q. And in 1929 were you the attorney for E. J. Lord, [35] Limited?

A. I was as under a regular retainer of E. J. Lord, Limited during the period, during the entire year of 1929.

Q. As a matter of fact you were the regular attorney under retainer of E. J. Lord, Limited, from its incorporation in 1926 to 1929?

A. I would not say exactly as to that, Mr. Wrenn, but I think it covered a period of at least two years.

Q. In 1929 were you consulted by Messrs. Black and Lord in regards to the redemption of capital stock of E. J. Lord, Limited, by the corporation?

A. I was. I was consulted by Mr. E. J. Lord, as president of E. J. Lord, Limited, and by Mr. Black, as one of its officers, and both of them comprising all of the stockholders with the exception of three, I think, each of whom held one share for the purposes of qualification in acting upon their directorate, at my office, touching the redemption of the stock then held and owned by Mr. Lord.

Q. Mr. Lord at that time held six hundred shares, didn't he, of the capital stock of E. J. Lord, Limited?

A. I think that is the correct figure.

Q. And Mr. Black four hundred shares?

A. Yes.

(Testimony of E. C. Peters.)

Q. Can you give us in detail just what E. J. Lord, Limited, was desirous of doing at that time in [36] regard to the stock which was owned by Mr. E. J. Lord?

A. Yes. The question first arose in the early part of December. Mr. Lord at that time was having domestic difficulties, his health was not too good, and Mr. Black was apprehensive of complications that might arise in the event of Mr. Lord's demise, and he came to the office and saw me about the proposition of the corporation acquiring and redeeming the stock then owned by Mr. Lord. I told Mr. Black that that was a matter he would have to take up personally with Mr. Lord; that, as controlling stockholders of the corporation, they would have to get together, and just as soon as they came to a mutual understanding as to the price on the one hand that Lord would expect to receive for his stock, and what the corporation on the other hand was willing to pay him for the redemption of his stock, that after they had arrived at a mutual understanding they were both to come to the office and discuss the situation. That was, as I say, along about the early part of December, and along about the 11th of December Mr. Lord and Mr. Black came to the office. The question then arose as to the *modus operandi*. I asked Mr. Black what the intentions of E. J. Lord, Limited, were, and particularly of himself, what they would be in the event of the elimination of Mr. Lord as a stockholder in the company. He told me he wanted it [37] arranged

(Testimony of E. C. Peters.)

so that the company acquire Mr. Lord's stock, and that just as soon as that stock was acquired and the consideration as ascertained paid to Mr. Lord, that the stock would be retired, and that the remaining shares of stock held by himself would represent the entire capital stock of the company. I asked him if he understood that as far as the situation was concerned that there were two methods of carrying forth what his and the company's desires were? One was the purchase of Mr. Lord's stock and its retention in the treasury as treasury stock and its subsequent disposition to others, if he desired to have increased capital in the corporation. The other method was to acquire the stock from Mr. Lord and retire that stock and reduce the capital of the corporation so that it was consistent with the value of the remaining stock. He told me that the latter method of the retirement of the stock and reduction of the capital stock was what he wanted, and on that basis I looked up what authorities were available to see just exactly what steps should be taken. The conference of December 11th resulted in an agreement between the corporation, on the one hand, and Mr. Lord on the other, that Lord was to receive what he had originally put into the corporation by way of contribution on the original organization, and that he was to also receive the undivided profits, [38] which, with the capitalization would represent the net worth of the business, and that net worth was to be computed as of the close of the year 1929, De-

(Testimony of E. C. Peters.)

cember 31st. The necessity of awaiting the closing of the books and the audit was apparent, and the net worth was adopted as the basis of computation due to the statement that Mr. Lord made at that time that certain articles of plant, which under the formula provided by the Engineers' Association, American Engineers' Association, that according to good bookkeeping had been wiped off the inventory, that there were certain articles of machinery and equipment that had thus been wiped off, and he wanted to be sure that the net worth as ascertained at the end of the year included every article of plant. So, whereas the plant might show one value upon an appraisalment and further investigation that value would have to be increased, so they were not closing on the basis of an actual net worth book value, but they were closing on a net worth value on which all the figures of the auditors and bookkeepers would be accepted, with the exception of inventory of plant. One of the items of consideration was the existing contracts E. J. Lord, Limited, at that time—

Mr. KAY: I have no objection to Judge Peters stating that these men, to-wit Mr. Lord and Mr. Black, approached him to draw up a contract, and he drew [39] up a contract pursuant to their request, but for Mr. Peters to testify as to what their intentions were and what they told him and all the surrounding facts of this transaction is to my mind clearly hearsay and immaterial as far as this witness is concerned and inadmissible. The documents

(Testimony of E. C. Peters.)

speak for themselves, and as far as the documents are concerned, if they are properly identified, there is no objection to their admission, but if Judge Peters' testimony is going to be a substitution for what Mr. Black and Mr. Lord would testify to, we would have to object, because we are entitled to our right of cross-examination of what their intentions were. We object to this line of testimony.

Mr. WRENN: I take it what the Board is after in this is to get down to really what happened at that time, at the time this transaction transpired, and to get the real intention of the parties. The testimony that Judge Peters is about to give, from a legal viewpoint, is entitled to be admitted, because it is part of the *res gestae*, things that occurred at the time the contract was entered into, and has a material bearing on the issue which is now being tried before the Board; but it seems to me, even though that is true as to a technical matter, part of the *res gestae*, the Board is interested in getting what was in the minds of the parties and how the attorneys proceeded to carry [40] these things out. I think it is clearly admissible on those grounds.

The CHAIRMAN: Objection overruled.

Mr. KAY: May we have our objection to this whole line of testimony, and exception to the ruling of the Board?

The CHAIRMAN: Certainly.

A. (Continuing.) As I was saying, the closing items for the year 1929 would not disclose Mr.

(Testimony of E. C. Peters.)

Lord's interest in certain contracts which E. J. Lord, Limited, had at that time, and which were incomplete, it being the accepted method and the particular method in the bookkeeping of E. J. Lord, Limited, as disclosed by Mr. Buchholtz, that whatever profits in any contract might accrue to the contractor, that the profits were not computed and entered in the books of the company until the final acceptance of the contract by the owner. All of these were public contracts and awaited acceptance by the authoritative officers of the Government,—so that the proposition was that Mr. Lord claimed that he was entitled to a percentage of profits that might accrue from those contracts, and hence, in addition to the consideration of sixty per cent. of the net worth of the business at the close of 1929, Mr. Lord said he was entitled to and Mr. Black on behalf of the company said it was willing to pay sixty per cent. of the profits [41] of certain outstanding contracts, when and as those contracts were completed and the profits computed; likewise as to any losses. So that on the 11th of December, 1929, at the time that this consultation was had with Mr. Lord and Mr. Black, it was agreed primarily that Mr. Lord was to receive sixty per cent. of the net worth of the business as it was disclosed at the end of the year and sixty per cent. of the profits that might accrue upon these contracts, a list of which Mr. Buchholtz was to furnish. I have a notation of the consultation. I have a sys-

(Testimony of E. C. Peters.)

tem in my office of making daily charge sheets, so that we can find out afterwards what we have done or refresh our memory as to what is done and make charges. Of course it doesn't mean we always get paid for that work, but we make the charges, nevertheless, and I have a memorandum as to that day, which I have picked out of my finished filed in the matter of the redemption of this stock for that day.

Q. Have you any objection to having this memo admitted in evidence?

A. Not at all, if it be of any value.

Mr. WRENN: We offer it in evidence.

Mr. KAY: We object to this. Mr. Lord and Mr. Black are proper witnesses on this matter.

Mr. WALSH: This is of no value to the Board.

Mr. WRENN: We submit it is of very material value [42] to the Board to show conclusively that on the 11th day of December, 1929, the corporation on one side, and Mr. Lord on the other side, had in mind the question of the corporation redeeming the capital stock he had at that time. This is an entry made contemporaneous with the discussions that took place at that time with Judge Peters, counsel for the corporation, indicating quite clearly that what was in the minds of the parties was a redemption of the stock of the corporation.

Mr. WALSH: Judge Peters has testified to that. This is merely a written confirmation of what occurred in his office. The real confirmation comes from the parties concerned.

(Testimony of E. C. Peters.)

Mr. WRENN: May we have this marked for identification?

(Document offered to be marked for identification received and marked: "Taxpayers' Exhibit 7 for identification.")*

Q. That entry was made by you on that day?

A. That entry was made by me on that day.

Q. And it was made at the close of the consultations which you had with Mr. Lord and Mr. Black on that day?

A. Yes. I want it distinctly understood that in this conference of December 11, 1929, I was acting for E. J. Lord, Limited. This entire work was done and charged against E. J. Lord, Limited, and paid for [43] by E. J. Lord, Limited, and prior to coming on the stand this morning Mr. Black, the president of E. E. Black, Limited, and successor of E. J. Lord, Limited, requested of me that I testify in this matter, and hence I am not violating any professional privilege. I think that was all that occurred on that day. There was, of course, considerable discussion. The memoranda will show that period of time in which Mr. Lord and Mr. Black were in my office. Mr. Lord and Mr. Black came back to the office the following day, the 12th of December, and it seems that the necessity of immediately drawing up this agreement had arisen. Mr. Black stated that Mr. Lord was contemplating going to San Francisco, and that he would like very

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

much to have an option drawn up reflecting the conversation and agreement of the day previous, and a contract was drawn up. Mr. MacComiskey was called into consultation on the question of Federal taxes. Mr. Buchholtz was called into consultation relative to the outstanding contracts and their identity and was asked to secure immediately the definite details of those contracts; and that was about ten o'clock in the morning when Mr. Lord and Mr. Black called. I was requested to have the contract ready by two o'clock. They came back again at two o'clock and there was some delay and finally, along about half-past four, the contract [44] was in final form. We had to wait for Mr. Buchholtz, as an officer of the company, to come down and sign it, and finally, as a notary, we secured Miss Sylvia Bryant, and the contract was concluded that afternoon. I made memoranda of what happened on that day. I won't say they are entirely complete, but they were sufficient for my purposes. (Witness produces papers.)

Mr. WRENN: I offer these three daily charge sheet memos dated December 12, 1929, in evidence.

Mr. KAY: Same objection as stated as to the other slip, and on the further ground evidently these slips are being introduced for the purpose of corroborating a matter that has not yet been presented to the Board. In other words, Judge Peters has been called out of order, if Mr. Wrenn intends to put on Mr. Black and Mr. Lord, and at that time

(Testimony of E. C. Peters.)

we will question them as to these conferences and what took place there,—I can see the materiality of Judge Peters' evidence, if it is material to the evidence in this case. Meanwhile, it seems to me this evidence is clearly hearsay and not admissible.

Mr. WRENN: This evidence is not out of order. It is perfectly in order, and it is perfectly competent, relevant and very important testimony,—perhaps the most important testimony we could offer; more important than relying upon the recollection [45] of this witness, and it certainly of course does corroborate what Judge Peters has been testifying to and indicates quite clearly the intention of the parties.

The CHAIRMAN: Objection sustained.

Mr. WRENN: I offer the three of them, then, as an exhibit for identification.

(Documents offered for identification received and marked: "Taxpayers' Exhibit 8 for identification.")*

Q. Have you with you here the final original contract that was prepared by you at the request of E. J. Lord, Limited, and Mr. E. J. Lord individually?

A. I have.

Q. Are you familiar with the handwriting of Mr. E. J. Lord?

A. I am. I have seen him write numerous times.

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Q. In your opinion is the signature on that contract the signature of E. J. Lord?

A. It is. I saw him sign it and saw Mr. Buchholtz sign on behalf of E. J. Lord, Limited, and saw them acknowledge their signatures before Sylvia Bryant.

Mr. WRENN: We offer the copy of the agreement dated December 13, 1929, between E. J. Lord of Honolulu and E. J. Lord, Limited, in evidence as Exhibit 7.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 7.") [46]

TAXPAYERS' EXHIBIT 9.

8 pages

(9)

FILED February 1, 1932

AT 11:40 o'clock A. M.

(s) ROBERT PARKER, JR.

Clerk Supreme Court.

THIS INDENTURE OF AGREEMENT made and entered into this 13th day of December, A. D. 1929 by and between E. J. LORD, of Honolulu, City and County of Honolulu, Territory of Hawaii, party of the first part, and E. J. LORD, LIMITED, an Hawaiian corporation having its principal place of business in said Honolulu, party of the second part,

WHEREAS the party of the first part is the owner of, and appears upon the stock books of the

(Testimony of E. C. Peters.)

party of the second part as the owner of six hundred (600) shares of the capital stock of the party of the second part, evidenced by certificates of stock of said party of the second part numbered 7, 8 and 9 for 310, 200 and 90 shares respectively, now outstanding in the name of the party of the first part; and

WHEREAS the party of the second part desires to redeem said shares of stock; and

WHEREAS the party of the first part is willing to accept as consideration for the sale of said stock to the party of the second part, and the said party of the second part is willing to pay to the said party of the first part for the redemption of said stock, a sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929 and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue to the party of the second part by its completion of the respective works contemplated by certain executory contracts to which the said party of the second part is a party, remaining uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which the party of the first part may become [274] liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and/or to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the

(Testimony of E. C. Peters.)

consummation of the sale of said six hundred (600) shares of the capital stock of said party of the second part; and

WHEREAS the net worth of the party of the second part cannot be determined until the books of the party of the second part have been closed for the year 1929 and an audit made thereof; and

WHEREAS the following enumerated contracts, to which the party of the second part is a party, remain uncompleted: Territory of Hawaii and City and County of Honolulu by Honolulu Sewer and Water Commission with E. J. Lord, Ltd., First section of Manoa-Kaimuki interceptor, dated July 16, 1928; City and County of Honolulu with E. J. Lord, Ltd., Improvement District Number 29, St. Louis Heights, dated August 20, 1929; Lyman H. Bigelow, Territorial Highway Engineer with E. J. Lord, Ltd., Kalanianaʻole Highway, F. A. Project No. 6A, Job #4034, dated (May 14, 1928) May 24, 1929; Territory of Hawaii by Board of Harbor Commissioners with E. J. Lord, Ltd., wharf and freight shed Pier #1 Nawiliwili, dated August 7, 1929; Territory of Hawaii by Board of Harbor Commissioner and E. J. Lord Ltd., Pier #2 Kapa-lama Basin, dated —————:

NOW, THEREFORE, THESE PRESENTS WITNESSETH:

That the party of the first part, in consideration of the sum of One Dollar (\$1.00) to him in hand paid by the party of the second part, the receipt

(Testimony of E. C. Peters.)

whereof is hereby [275] acknowledged, and the covenants and agreements of the party of the second part hereinafter contained, on its part to be kept and performed, does hereby and by these presents:

1. Give and grant to the party of the second part an option, irrevocable within the time for acceptance herein limited, to purchase free from encumbrances the said six hundred (600) shares of the capital stock of the party of the second part so owned by him and so evidenced and so outstanding as aforesaid for the consideration hereinafter set forth.

2. Assign and deliver unto the said party of the second part six hundred (600) shares of the capital stock of the party of the second part so owned, evidence and outstanding as aforesaid, duly endorsed by him on the back thereof to the order of the party of the second part by way of pledge to secure the performance by him of the covenants and agreements hereof on his part to be kept and performed, and does constitute and appoint the said party of the second part his true and lawful attorney for him and in his name and stead, upon the exercise of the option hereby granted by the party of the second part, to cause said six hundred (600) shares of the capital stock of the party of the second part to be redeemed by the said party of the second part and the same to be recorded on the proper books of the party of the second part.

And in consideration of the covenants and agree-

(Testimony of E. C. Peters.)

ments of the party of the first part hereinbefore contained and the sum of One Dollar (\$1.00) in hand paid by the party of the first part to the party of the second part, the receipt whereof is hereby acknowledged, the party of the second part [276] does hereby and by these presents covenants and agrees by and with the party of the first part as follows:

1. That it will, as soon as may be, at its own proper cost, cause its books to be closed as of December 31, 1929 and cause the same to be admitted by a competent auditor or competent auditors.

2. That it will, as soon as may be, at its own proper cost, fully perform and complete the work respectively contemplated by the pending contracts hereinbefore enumerated, to which it is a party, in a workmanlike and economical manner, and will, as soon as may be, reduce to possession all moneys, bonds or other consideration accruing and payable or deliverable to it thereunder.

3. That it will keep and have open for the inspection of the party of the first part at its place of business full and complete books of account of the receipts and disbursements respectively made and received by it on account of said pending contracts.

4. That said party of the second part, upon the exercise of the option by it to it hereby granted, will, as soon as may be, cause its articles of association to be amended so that its name does not con-

tain the name "E. J. Lord" or any part of said name, or contain any words similar to said name "E. J. Lord" or any part thereof.

And the parties hereto, in consideration of their status hereunder, mutually covenant and agree;

1. That the option hereby given shall be open for acceptance up to, but not after the 28th day of February, 1930, and may be accepted by letter delivered to the party of the first part or mailed, postage prepaid and registered, addressed [277] to the party of the first part at his residence at Dowsett Highlands, Honolulu.

2. That the purchase price of the said stock of the party of the second part shall be a sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929 and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue to the party of the second part by its completion of the respective works contemplated by said pending contracts, to which it is a party, now remaining uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which the party of the first part may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock of the party of the second part. That

(Testimony of E. C. Peters.)

such purchase price shall be paid to the party of the first part at the time and in manner following, that is to say: the sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929 forthwith upon the exercise by the party of the second part of the option hereby granted to it. In the event that the amount so payable exceeds the sum of Two Hundred Fifty Thousand Dollars (\$250,000.00), the amount of the excess over that sum may be retained by the party of the second part until and paid by it to the party of the first part upon the completion of the St. Louis Heights contract and the receipt by it of the full consideration for the performance thereof; [278] the sum of money equal to sixty per cent (60%) of the net profits yet to accrue from each of the foregoing enumerated uncompleted contracts when completed and the moneys, bonds or other consideration accrued and payable or deliverable to the party of the second part thereunder, reduced to possession, and the sum of money equal to forty per cent (40%) of the income tax to which the party of the first part may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued or to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock of the party of the second part, forthwith upon assessment.

(Testimony of E. C. Peters.)

3. That if any dispute or difference shall arise and exist between the parties hereto in respect to any provision hereof, said dispute and cause of difference shall be referred and submitted to the arbitration and determination of three persons, two of whom shall be accountants and one of whom shall be an engineer; that the parties hereto now nominate and appoint as such arbitrators, H. Douglas Young, an accountant, J. K. Lamberton, an accountant, and Fred E. Harvey, an engineer. In case any of such arbitrators shall die or refuse or become incapable to act as arbitrator, substitution shall be made from the following named alternates, such substitute to be of the same profession as the arbitrator for whom he is substituted. The parties hereby nominate as alternates, Fred G. Pearson, an accountant, L. N. MacComiskey, an accountant, and J. L. Young, an engineer. Any substitute arbitrator shall have the same powers and authority as the arbitrator first appointed hereunder, for whom he is substituted, would have had if he had acted on *con-* [279] *be* final as between the parties hereto and shall in all respects be kept and faithfully observed by them and neither party hereto shall bring or prosecute any action against the other nor against the arbitrators nor any of them concerning the matter in difference or any of them concerned in any reference. The cost of any arbitration shall be borne equally by the parties hereto.

(Testimony of E. C. Peters.)

4. That time is of the essence hereof.

5. That the term “party of the first part” wherever employed herein, when agreeable to the context, shall be understood to mean and include the party of the first part and his executors, administrators and assigns, and that the term “party of the second part” shall be understood to mean and include the party of the second part, its successors and assigns.

IN WITNESS WHEREOF, the party of the first part has set his hand and seal and the party of the second part has caused its name to be hereunto subscribed and its corporate seal affixed hereto and to another instrument of like date and tenor by its proper officers thereunto duly authorized, the day and year first above written.

[Seal] E. J. Lord.
E. J. LORD, LIMITED.

[Seal] By E. E. Black,
Vice-President.
Geo. Buchholtz,
Treasurer.

[280]

City and County of Honolulu
Territory of Hawaii—ss.

On this 13th day of December, A. D. 1929, before me personally appeared E. J. LORD, to me known to be the person described in and who executed the

(Testimony of E. C. Peters.)

foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal]

SYLVIA LESLIE BRYANT,
Notary Public, First Judicial Circuit,
Territory of Hawaii.

City and County of Honolulu
Territory of Hawaii—ss.

On this 13th day of December, A. D. 1929, before me appeared E. E. BLACK and GEORGE BUCHHOLTZ, to me personally known, who being by me duly sworn, did say that they are the Vice-President and Treasurer respectively of E. J. LORD, LIMITED, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. E. Black and George Buchholtz acknowledged said instrument to be the free act and deed of said corporation.

[Seal]

SYLVIA LESLIE BRYANT,
Notary Public, First Judicial Circuit,
Territory of Hawaii. [281]

Q. After the execution of this agreement did you have any further conferences as to the redemption of Mr. Lord's stock by E. J. Lord, Limited, with Mr. Lord and Mr. Black?

A. I did.

(Testimony of E. C. Peters.)

Q. When was the next conference, as your records show?

A. The next conference I had with Mr. Lord and Mr. Black was on the day following.

Q. What was that conference about?

A. I have no,—I haven't any particularly clear recollection of what occurred on the 13th of December. I have a notation in the handwriting of my stenographer, and I have my own handwriting which I must have made after their departure, "E. J. Lord and Mr. Russell called re option Lord."

Mr. WALSH: You mean the 14th, don't you?

A. Yes, that's true. The memoranda on the 12th that I speak of do not refer to the details of the calling of Mr. Lord and Mr. Black on the 13th, when they called in the morning and the contract was drafted, and they came in in the afternoon and executed it. The details of the 12th were further discussions, somewhat along the same lines as the 11th. I remember that Mr. Russell came in with certain grammatical suggestions relative to the contract and they were accepted and the contract was executed in its final form such as you have [47] offered and admitted in evidence.

Q. This Mr. Russell you refer to is Mr. Russell of Davies & Company?

A. Yes, Mr. Russell of Davies & Company.

Q. And he was consulted at the suggestion of Mr. Black to look over this contract?

A. Yes, Mr. Russell, as I understood from Mr. Black, was to assist E. J. Lord, Limited, in what-

(Testimony of E. C. Peters.)

ever financing was required, and I asked Mr. Black on the day we drafted the contract to go down and see Mr. Russell and show it to him, and, if he desired to consult with Mr. Edmondson, an attorney at law associated with Mr. Russell.

Q. The entries on this charge sheet of December 14, 1929, are in your handwriting?

A. Yes, and made by me at the time.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained.

Mr. WRENN: I offer this to be marked for identification.

(Document offered to be marked for identification received and marked: "Taxpayers' Exhibit 10 for identification.")*

Q. When were you again consulted by either of these two gentlemen?

A. I was consulted from time to time, but they were mere details in the consummation of the agreement. For instance, in the latter part of December [48] the question arose over the auditors who had been employed for the purpose of ascertaining this net worth, the question arose as to what charges for depreciation on the one hand, or rental on the other, should be charged on plant that was devoted to the completion of these uncompleted contracts, and there was a consultation with Mr. Lord and there was consultation with Mr. Buchholtz and

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. Black and it finally resulted in a letter to Messrs. Young, Lambertson and Pearson as to how to handle that matter, and memorandum was made as of the 23d and 26th in that regard.

Mr. WRENN: We offer each of these memoranda.

Q. These memos are in your handwriting and made on these respective dates?

A. The words "Mr. Buchholtz" and "Mr. Black" are written by my stenographer. The way that occurs is the stenographer, when a person calls, makes an entry of the name and date and—

Q. The words here "Redemption of stock" are in your handwriting?

A. In my handwriting made at the time of the call, similarly as to the slip of December 23d.

Mr. WRENN: I offer in evidence slip of December 23, 1929.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained. [49]

Mr. WRENN: Exception, and I offer it to be marked for identification.

(Document offered for identification received and marked: "Taxpayers' Exhibit 11 for identification.")*

Mr. WRENN: I offer in evidence memorandum of December 26, 1929.

Mr. KAY: Same objection.

The CHAIRMAN: Sustained.

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. WRENN: Exception, and I offer it for identification.

(Document offered for identification received and marked: "Taxpayers' Exhibit 12 for identification.")*

Mr. WRENN: Q. And the memo of December 27, 1929, the redemption of stock, E. J. Lord, that is in your handwriting?

A. Yes.

Mr. WRENN: I offer that in evidence.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained.

Mr. WRENN: Exception, and I offer it for identification.

(Document offered for identification received and marked: "Taxpayer's Exhibit 13 for identification.")*

Q. Mr. Buchholtz at that time was treasurer of E. J. Lord, Limited?

A. He was, and was handling the retails of the [50] closing items. We were waiting upon Mr. Buchholtz to close the books, and particularly to get up an itemization of plant account. That seemed, in December and January, to be the burden of Mr. Lord's calls at the office, and Mr. Buchholtz. For instance, I have a notation in my handwriting, with the exception of the date and Mr. Buchholtz' name, On January 20th 1930, "Mr. Buchholtz called re valuation." It harped back to that original thought

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

of determining Mr. Lord's interest from a net worth value which actually reflected the true and not on any arbitrary net worth as reflected by the books, including this plant account, many articles of which it was pointed out by Mr. Lord had been used on contracts and the period of their life had lapsed, and for that reason they had been dropped from the plant account and Mr. Lord was anxious to receive every dollar of interest to which he was entitled in those portions of the plant, and that did not appear on the plant account of the books, and Mr. Buchholtz called on the 20th of January.

Q. Mr. Buchholtz was thoroughly familiar with the transactions and the corporation's desire to redeem the stock?

A. Mr. Buchholtz was thoroughly familiar with what was going on. The matter had been discussed between [51] himself and myself for the purpose of his having clearly in mind what was the arrangement between Mr. Lord and Mr. Black, so he could pursue his duties as treasurer of the corporation. Accordingly on the 23d of January Mr. Buchholtz called at the office again, on the 21st of January he having filed with me his first statement of what the books reflected upon the closing entries of the year 1929, and he told me at that time that there were still matters he had to get in, but it was in rough shape and we went over again the question of net worth. I have my memorandum, "Mr. Buchholtz in re statement of net worth, December 21, 1929," and that matter continued until I had a

(Testimony of E. C. Peters.)

conference with Mr. Black. I told him Mr. Lord was dissatisfied with the inventory of plant; that he was dissatisfied with the valuation of plant, and that under all the circumstances I would advise that some independent person be called in in regard to the value of the plant. Mr. Black demurred to that. He said he thought Mr. Lord was over captious. He felt that the book value of the plant as it was was in excess of its actual value, but he said if Mr. Lord wanted to question that valuation it was all right with him, and Mr. Fred Williams was employed,—formerly of Aiea, Waipahu and Waialua plantation, and he proceeded with an inventory of plant and report upon it was finally filed with me and called to the attention of Mr. [52] Black and Mr. Lord on the 3d of April 1930; so that from the time of the closing of the books on December 31st and until that time, April of 1930, the question of valuation of plant was still a matter of discussion. In the meantime I had drafted, pursuant to the contract a petition for amendment of the articles of association of E. J. Lord, Limited, changing the name to E. E. Black, Limited, and in that regard I should like to say that this matter of E. E. Black, Limited, came up for discussion in the first preliminary meetings. Mr. Black insisted that as long as this stock was to be retired, and he was practically to be the sole owner of the business, he wanted a change of name to E. E. Black, Limited, and Mr. Lord, on the other hand, felt that was proper and also felt that he perhaps might de-

(Testimony of E. C. Peters.)

sire to embark in business for himself and it was better that E. J. Lord, Limited, change its name.

(Recess)

Q. During the recess I brought to your attention a copy of a letter addressed to Young, Lambertson & Pearson dated December 30, 1929. Is that the letter you stated as having been drawn by you advising the auditors of the transaction?

A. It is. I have a carbon copy if Mr. Kay would like to look at it. This carbon copy in my folder which would be the same as the original. [53]

(Witness produces paper)

Mr. WRENN: I offer it in evidence as Exhibit 14.

Mr. KAY: That will carry our objection in mind we are objecting to all this line of testimony as to immateriality and incompetency.

The CHAIRMAN: Objection overruled.

(Document offered in evidence received and
Marked "Taxpayers' Exhibit 14.")

TAXPAYERS' EXHIBIT 14.

(14)

December 30, 1929

Young, Lambertson & Pearson

Honolulu, T. H.

Gentlemen:

In the Matter of the Redemption Contract
between E. J. Lord, Ltd. and E. J. Lord,
dated December 13, 1929.

Mr. Buchholtz, our treasurer, has been instructed to charge each job in which Mr. Lord has an inter-

(Testimony of E. C. Peters.)

est, subject to the above marginal contract, with the value of the use of plant belonging to the company in accordance with the rates contained in the column entitled "Expense Per Working Month Per Cent" in the "Construction Equipment Schedule" found on page three of the publication of the Associated General Contractors of America Inc., 1038 Munsey Building, Washington, D. C., copyrighted 1927, entitled "Construction Equipment, a Report on Current Practice Pertaining to Construction Equipment, Including an Equipment Schedule, a Rental Agreement, Equipment Record and other Forms."

Respectfully yours,

E. J. LORD, LTD.

By—(Sgd.) E. E. BLACK.

By—(Sgd.) E. J. LORD. [282]

Q. I call your attention to a receipt dated February 15, 1930. Did you prepare this receipt?

A. Yes. Mr. Buchholtz called at the office and had a rough draft of receipt that he had prepared which contained the same figures and notes and bonds as contained in the receipt as finally drafted, and after a discussion of the matter I drew this receipt for him to sign,—to get Mr. Lord's signature to it, with certain instructions that he should advise Mr. Lord in respect to. The receipt afterwards I saw again with Mr. Lord's signature. I didn't see Mr. Lord sign this receipt, but that is his signature.

(Testimony of E. C. Peters.)

Mr. WRENN: I offer the receipt in evidence as Exhibit 15.

Mr. KAY: That carries our same objection we have interposed here to the whole line.

Mr. WRENN: That is the receipt showing payment by E. J. Lord, Limited, to E. J. Lord of the first installment under the contract.

The CHAIRMAN: Objection overruled. [54]

(Document offered in evidence received and marked: "Taxpayers' Exhibit 15.")

TAXPAYERS' EXHIBIT 15.

pages 1-2 (15)

Honolulu, Hawaii, February 15, 1930.

E. J. Lord, Limited having duly accepted the option granted by me to it by the indenture of agreement between us dated December 13, 1929, and the sum of Two Hundred Seventy-three Thousand Eight Hundred Fifty-five Dollars and Thirty-six cents (\$273,855.36) having been found to be sixty (60%) of the net worth of E. J. Lord, Limited as of December 31, 1929;

I hereby accept in lieu of cash and acknowledge receipt from E. J. Lord, Limited in payment of the sum of Two Hundred Fifty Thousand Dollars (\$250,000.00) on account of the purchase price of the six hundred (600) shares of the capital stock of E. J. Lord, Limited, the subject of said indenture, the following enumerated notes, bonds and cash:

(Testimony of E. C. Peters.)

Note Honolulu Iron Works @ 5½% \$ 50,000.00

Due 4/15/30

Interest from 1/1/30 payable direct to

E. J. Lord

Note Hawaiian Trust Co. @ 6½% \$ 50,000.00

payable on demand

Interest from 1/1/30 payable direct to

E. J. Lord

Bonds: St. Louis Hghts. Impr. Bonds 119,000.00

@ 5% Tax free

Coupons 2-18 attached from 2/15/30

(Interest see below)

Bonds: Lihue Plant. Co. Bonds @ 5½% 15,000.00

Coupons 6-20 attached from 2/15/30

(Interest see below)

Bonds: Seattle Lighting Co. Bonds 15,000.00

@ 5%

Coupons 41-80 attached from 10/1/29

(Interest see below)

Check for Balance 1,000.00

\$250,000.00

E. C. PETERS

Attorney at Law

Alexander & Baldwin Bldg.

Honolulu, Hawaii

(Testimony of E. C. Peters.)

I also hereby acknowledge the receipt from E. J. Lord, Limited of the sum of Six Hundred Fifty-six Dollars and Twenty-five Cents (\$656.25) interest on said bonds from January 1, 1930 to date in lieu of interest coupons covering said period computed as follows:

Interest payable to E. J. Lord	\$743.75
--------------------------------	----------

St. Louis Hghts. 1/1/30 to 2/15/30	
------------------------------------	--

11½ months	
------------	--

Interest payable to E. J. Lord	68.75
--------------------------------	-------

Lihue Pl. Co. 1/1/30 to 2/1/30	
--------------------------------	--

1 month	
---------	--

	\$812.50
--	----------

Less: Interest accrued	156.25
------------------------	--------

Seattle Lightg. Co. 10/1/29 to	
--------------------------------	--

1/1/30, 3 months	
------------------	--

	\$656.25
--	----------

(Sgd.) E. J. LORD.

E. C. PETERS

Attorney at Law

Alexander & Baldwin Bldg.

Honolulu, Hawaii

Receipt of Settlement with E. J. Lord \$250,000.00
2/15/30. [284]

(Testimony of E. C. Peters.)

Q. Just prior to the recess you spoke of handling for E. J. Lord, Limited, the matter of change of name to E. E. Black, Limited?

A. Yes. I drew a petition for the amendment of the articles of association of E. J. Lord, Limited. I drew up the minutes for the meeting of stockholders of E. J. Lord, Limited, and drafted a letter of instructions to Mr. Buchholtz as to what was to be done, and the meeting was held and petition signed and I finally sent it to the treasurer's office.

Q. I call your attention to Exhibit 2. Is that the petition you prepared at that time?

A. That is the petition. It is on my stationery.

Q. Why was it that you did not petition the treasurer of the Territory at that time for authority to reduce the stock?

A. The amount that was coming to Mr. Lord had as yet not been determined upon. The option required a certain payment to be made within a certain time and this payment, receipt for which is dated February 15, 1930, was the preliminary payment required by the option. If I might call to your attention that question of finances was a discussion matter of ~~discretion~~ on the 11th and 12th of December, and it was incorporated in the contract which the Board [55] will find on page 5. To pick up the thread,—“That such purchase price thereby paid to the party of the first part at the time and in manner following, that is to say an amount of

(Testimony of E. C. Peters.)

money equal to the net worth to the party of the second part as of December 31, 1929, forthwith upon the exercise by the party of the second part of the option hereby granted to it." The option was to December 31, 1930, and not sooner, but there was a letter written, I think, by the E. J. Lord, Limited, to Mr. Lord stating that the company exercised the option long prior to the time limitation. "In the event the amount so payable exceeds the sum of \$250,000. the amount of the excess over that sum may be retained by the party of the second part and paid by it to the party of the first part upon the completion of the St. Louis Heights Contract" etc., "and the receipt by it of the full consideration for the performance thereof."

The first payment of \$250,000. evidenced by that receipt was made by this provision of the contract, but the actual amount which was coming to Mr. Lord, and the amount by which the capital stock of E. J. Lord, Limited, would be reduced, could not be ascertained until these five or six incompleated contracts were completed, and then for the first time the books would take up the slack and make the closing entries, which would disclose the profits. [56]

Q. This reduction of the capital stock was made in the early part of 1931, after the final settlement with Mr. Lord?

A. Yes, it was. I might say in regard to that on the 27th of February, I think it was, 1930, E. J. Lord, Limited, for economical reasons sus-

(Testimony of E. C. Peters.)

pended the retainer which they, up to that time, had paid me, to take effect on the 28th of February, 1930. I thought Mr. Black might have waited until the end of March and not take advantage of just one day, but he closed it up on the 28th of February, and there were several inventory matters that spread down into the early part of 1931 for this reason. This question of plant became acrimonious as between Mr. Black and Mr. Lord, and I finally called Mr. Lord and Mr. Black in and said "Here, I have been representing E. J. Lord, Limited, in all these transactions. It has been satisfactory right straight along. Both of you gentlemen have been satisfied with my performances in the matter, but if you are going to get into a quarrel about this plant account you gentlemen will have to get somebody else." Black said he didn't want anybody else and wanted me to try to settle the thing up. I told him I couldn't do anything about it, I had represented Mr. Lord for years, I have the pleasure and privilege of his employment, and I didn't want to get in any [57] quarrel with the gentleman, and finally Mr. Lord came in and told me he had seen Mr. Thompson's office relative to it, and in August of 1930,— We had gone right along. They had this back and forth and some of it was hot and some of it was cold, but finally on the 6th of August I turned over the matter of the appraisement to Mr. Beebe. Then along towards the Fall,—in the meantime Mr. Lord was represented by the Hawaiian Trust Company as to his financial affairs, and Mr.

(Testimony of E. C. Peters.)

Black, as I understood it, had employed Judge Robertson's office. I could very easily see that there was going to be extended difficulties, and you must remember that during this time I was still representing Mr. Lord in his domestic affairs. There was a libel and cross-libel pending. I wanted to get his affairs settled up. I didn't want any more loose thread hanging, and I finally enlisted the services of the Hawaiian Trust Company by Mr. Peter McLean to get together with Mr. Lord and Mr. Black and the whole bunch decide that question of valuation. So finally, as my recollection serves me, in the early part of January or February the dove-of-peace was finally supreme, and this question was finally disposed of. Then the next thing,— Of course in the meantime I had ceased to be the attorney for E. J. Lord, Limited, and I noticed that within a very short time after the difficulties had been ironed [58] out, I noticed in the papers that E. J. Lord, Limited, applied to the Treasurer to reduce its capital stock, and that was the final step in the negotiations that began on December 11th in 1929.

Q. I call your attention to a receipt dated December 26, 1930, and the signature on that receipt?

A. Yes, I recognize both Mr. Buchholtz' and Mr. Lord's handwriting. I have seen Mr. Buchholtz sign his name upon numerous occasions.

Mr. WRENN: I offer receipt in evidence as Exhibit 16.

Mr. KAY: Same objection made as to all this line of testimony.

(Testimony of E. C. Peters.)

The CHAIRMAN: Objection overruled.

Mr. KAY: Exceptions.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 16.")

TAXPAYERS' EXHIBIT 16.

3 pages (16)

THIS AGREEMENT, made this 26th day of December, 1930, by and between E. E. BLACK, LIMITED (successor in name to E. J. LORD, LIMITED), an Hawaiian corporation, party of the first part, and E. J. LORD, of the City and County of Honolulu, Territory of Hawaii, party of the second part,

WITNESSETH:

That the party of the first part, in consideration of the transfer and delivery to it of six hundred (600) shares of the capital stock of said E. E. Black, Limited, by the party of the second part, does hereby assign, transfer and deliver to the party of the second part, the following bonds:

One hundred thirty-six (136) St. Louis Heights Improvement Bonds (par value \$500.00 each) with coupons attached from August 15, 1930,	\$ 68,000.00
Ten (10) Arkansas Light and Power Co. Bonds (par value \$1000.00 each) with coupons attached from October 1, 1930,	10,000.00
Ten (10) Alabama Power Co. Bonds (par value \$1000. each) with coupons attached from December 1, 1930,	10,000.00

(Testimony of E. C. Peters.)

Ten (10) Texas Power and Light Co. Bonds (par value \$1000. each) with coupons attached from November 1, 1930,	10,000.00
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Nine (9) Emporium Capwell Corpora- tion Bonds (par value \$1000. each) with coupons attached from October 1, 1930,	9,000.00
---	----------

\$107,000.00

And does hereby pay to said party of the second part in cash, the sum of	67,036.12
with interest thereon from July 31 to December 31, 1930, at the rate of two per cent (2%) monthly	670.36

Also interest accrued on the above men-
tioned bonds since August 1, 1930, as
follows:

St. Louis Heights Improvement Bonds $\frac{1}{2}$ month at 5%	141.67
--	--------

(Forward)	\$174,848.15
	[285]

(Brought forward)	\$174,848.15
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Arkansas Light & Power Co. 2 months at $5\frac{1}{2}\%$	91.66
--	-------

Alabama Power Co. 4 months at 5%	166.67
-------------------------------------	--------

Texas Power & Light Co. 3 months at 5%	125.00
---	--------

Emporium Capwell Corporation, 2 months at $5\frac{1}{2}\%$	82.00
---	-------

\$175,313.98

(Testimony of E. C. Peters.)

AND the party of the second part does hereby acknowledge receipt of the above mentioned bonds and cash aggregating the value of \$175,313.98, as full and final payment for said 600 shares of the capital stock of E. E. Black, Limited, and in complete settlement of the agreement made between said E. J. Lord and E. J. Lord, Limited, dated the 13th day of December, 1929, except as hereinbelow stated.

IT IS MUTUALLY UNDERSTOOD AND AGREED as follows:

1. That this settlement is based upon the assumption that the federal income tax upon the profits of E. E. Black, Limited, on the contracts mentioned in the said agreement of December 13, 1929, will amount to the sum of Ninety-five Thousand Five Hundred Sixty-seven and 93/100 Dollars (\$95,567.93), and that if upon the assessment of said taxes being made it shall develop that the amount thereof is more or less than said sum the parties hereto will make an adjustment whereby the one shall pay to the other such sum of money as will make up the difference.

E.E.B.Ltd.

G.B.

E.J.L.

2. And that the party of the first part will pay forty per cent (40%) of the federal and Territorial income tax which shall be assessed against the party of the second part by reason of and resulting [286] from the sale and transfer by him of said shares of E. E. Black, Limited.

(Testimony of E. C. Peters.)

IN WITNESS WHEREOF the said E. E. Black, Limited has caused its name and corporate seal to be set by its Treasurer thereunto duly authorized, and the said E. J. Lord has set his hand, hereunto and to another instrument of like date and tenor, the day and year first above written.

E. E. BLACK, LIMITED.

[Seal] By (Sgd.) GEO. BUCHHOLTZ,
Its Treasurer.

(Sgd.) E. J. LORD.

[Endorsed]: Final Settlement between E. E. Black, Ltd. and E. L. Lord 12/26/30. [287]

Q. Can you recall at this time any other discussions or transactions between the parties which throws any light on this situation?

A. I have a memorandum here in the same manner, same file, with my notations upon it, under date of February 17th, that "Mr. Lord and Mr. Black and Mr. Buchholtz called re valuation of plant. Buchholtz will get up list." I remember that. It was a question as to whether or not the plant account as contained in the books contained all the plant, [59] and I think Mr. Buchholtz was to get up a list of not only what was contained in the plant account but what might be in the yards or on any job. That was under date of February 17, 1930. I have a notation under date of February 25, 1930, "Conference with Mr. Lord and Mr.

(Testimony of E. C. Peters.)

Williams and conference re appraisement of plant of E. J. Lord, Limited." That is in relation to the employment of Mr. Williams. That is under the date of the 25th and Mr. Williams called in again the same day. The Hawaiian Trust was handling Mr. Lord's affairs in July. As early as July Peters got into the proposition,— Later on in the Fall of the year for the purpose of settlement, for I have a notation here that Mr. Buchholtz 'phoned me July 15th if certain bonds were to be delivered to me or to the Hawaiian Trust Company, and I told him to deliver them to the Hawaiian Trust. I have a distinct recollection of that, and find it on July 15th, 1930. The time it was turned over to Beebe is refreshed by a memorandum under date of August 5, 1930, "Conference with Lord and Beebe" and that hinges up with my evidence relative to Lord getting someone else to represent him independently, and I have on my slip it was conference with reference to retirement of stock.

Q. You made that on the date it indicated?

A. That is in my handwriting. [60]

Mr. WRENN: I offer this in evidence.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained.

Mr. WRENN: Exception. I offer it to be marked for identification.

(Document offered to be marked for identification received and marked: "Taxpayers' Exhibit 17 for identification.")*

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. KAY: May it please the Board, we at this time move to strike the testimony of this witness on the ground that it is incompetent, irrelevant and immaterial, and the matters testified to are in the possession and knowledge of the officers of E. J. Lord & Company, to-wit, Mr. Black and Mr. Lord who are present in the court room. The evidence thus far adduced, whatever value it may have, is of a secondary nature, and the proper way, as I see it, to proceed, would be to call Mr. Black and Mr. Lord on these matters.

The CHAIRMAN: Motion denied.

Mr. KAY: Exception.

(Cross-examination waived.)

Mr. WRENN: I asked Mr. Glass if he would produce the original tax returns of E. J. Lord, Limited, for the calendar years 1926, 1927, 1928 and 1929. I offer in evidence the Territorial corporation income tax return for the 12 months preceding January 1, 1927, of E. J. Lord, Limited. [61]

(Document offered in evidence received and marked: "Taxpayers' Exhibit 18.")*

Mr. WRENN: I offer in evidence Territorial Corporation income tax return for the 12th months preceding January 1, 1928, of E. J. Lord, Limited.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 19.")*

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. WRENN: I offer in evidence corporation income tax return, Territory of Hawaii, E. J. Lord, Limited, for the 12 months preceding January 1, 1929.

(Document offered in evidence received and marked "Taxpayers' Exhibit 20.")*

Mr. WRENN: I offer in evidence corporation income tax return for the 12 months preceding January 1, 1930, Territory of Hawaii, E. J. Lord, Limited.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 21.")*

Mr. WRENN: And the corporation income tax return for the Territory of Hawaii for the 12 months preceding January 1, 1931, of E. E. Black, Limited.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 22.")*

Mr. WRENN: I assume that the income tax return of E. J. Lord personally for the 12 months preceding January 1, 1931, is part of this record. And is the amended tax return of E. J. Lord for the twelve months preceding January 1, 1931, also a part of the record? [62]

*Omitted from printed record on stipulation by counsel.

GEORGE BUCHHOLTZ

was duly called and sworn as a witness for the Taxpayer, and testified as follows:

Direct Examination by Heaton L. Wrenn, Esq.

Q. What is your name?

A. George Buchholtz.

Q. You are the secretary and treasurer of E. J. Lord, Limited?

A. I am.

Q. And prior to the amendment of the articles of incorporation, changing the name to E. E. Black, Limited, you were treasurer of E. J. Lord, Limited?

A. I was.

Q. And you were the treasurer of E. J. Lord, Limited, from the time of its incorporation in 1926?

A. Yes, sir.

Q. Prior to the incorporation of E. J. Lord, Limited, you had been the bookkeeper for Mr. E. J. Lord, hadn't you?

A. Yes.

Q. And you compiled the figures which are the exhibit to the articles of incorporation showing the condition of affairs prior to incorporation and at the time of incorporation?

A. Yes.

Q. During the time you were treasurer of E. J. Lord, Limited, you had general supervision of the book accounts of the corporation, didn't you? [63]

A. Yes.

Q. And you still have of E. E. Black, Limited?

A. Yes.

(Testimony of George Buchholtz.)

Q. Have you the Territorial income tax receipts showing payment of Territorial income taxes of E. J. Lord, Limited, for the 12 months preceding January 1, 1927?

A. Yes

Mr. WRENN: I offer two receipts showing payments of taxes for first half and second half as one exhibit.

(Documents, consisting of six sheets, offered in evidence received and marked: "Taxpayer's Exhibit 23.")*

Mr. WRENN: I offer in evidence Territorial corporation income tax receipts for E. J. Lord, Limited, for the 12 months preceding January 1, 1928. These also show receipts for property taxes.

(Documents offered in evidence, consisting of eight sheets, received and marked: "Taxpayer's Exhibit 24.")*

Mr. WRENN: I offer in evidence two receipts showing payment of Territorial income tax receipts for the Territory for 12 months preceding January 1, 1929. These receipts also show payment of property taxes.

(Documents offered in evidence, consisting of nine sheets, received and marked: "Taxpayer's Exhibit 25.")* [64]

Mr. WRENN: I offer two receipts showing payment of Territorial income taxes of E. J. Lord,

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

Limited, for twelve months preceding January 1, 1930.

(Documents offered in evidence, consisting of four sheets, received and marked: "Taxpayer's Exhibit 26.")*

Mr. WRENN: I offer in evidence Territorial corporation income tax receipt for E. E. Black, Limited, for the twelve months preceding January 1, 1931, first half.

(Document offered in evidence, consisting of one sheet, received and marked: "Taxpayer's Exhibit 27.")*

Q. Has E. E. Black, Limited, paid the second half of its Territorial income tax?

A. Yes, it has.

Q. Have you the receipt?

A. I haven't it here. I don't know that I have it in the office. The reason for that is there was a dispute as to the property tax, I haven't it here. I can give you the date and the amount that was paid.

Q. Will you do that, please.

A. Dated November 13th.

Q. What is the amount of the taxes?

A. \$15,128.40.

Q. That is the latter part of the taxes for the [65] twelve months preceding January 1, 1931?

A. Yes.

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

Q. Do you recall in the latter part of 1929 a discussion between E. J. Lord, Limited, a corporation, on one side, and Mr. E. J. Lord, relative to the retirement of the capital stock in E. J. Lord, Limited?

A. I do.

Q. At that time Mr. E. J. Lord owned 600 shares of the capital stock of E. J. Lord, Limited?

A. Yes.

Q. And Mr. Black 400 shares?

A. Yes.

Q. And it was capitalized at \$100,000.?

A. Yes.

Q. What was the plan of the corporation at that time for redeeming the stock held by Mr. E. J. Lord?

A. Well, the company wanted to redeem that stock, but as our books show he closed off each share on the completed contract basis, and Mr. Lord was interested in all the uncompleted contracts which we had on hand on December 31, 1929. Some of those contracts were not completed until the latter part of the year. Therefore, there was only one possibility, as far as I could see; in fact, I took the thing up with Young, Lambertson & Pearson, our attorneys, how to handle the thing.

Q. Was the plan at that time to redeem as soon as [66] you had cash available the 600 shares of stock held by Mr. E. J. Lord?

A. Yes.

(Testimony of George Buchholtz.)

Q. And after that stock had been fully redeemed for the corporation to retire the stock by reduction of its capital and cancellation of the stock so redeemed from Mr. Lord?

A. I didn't get your question.

Q. Was it the plan of the corporation after it had fully redeemed Mr. Lord's stock, when cash became available, for that purpose, to then petition the Treasurer for reduction of its capital?

A. Yes, as soon as the deal was completed.

Q. To reduce its capital to forty thousand dollars?

A. To reduce its capital to forty thousand.

Q. And to cancel the stock redeemed from Mr. E. J. Lord?

A. Yes.

Q. And you took a prominent part in the negotiations, didn't you, between E. J. Lord, Limited, and Mr. E. J. Lord in regard to this transaction?

A. Yes.

Q. And, as I understand it, you compiled the figures that had to do with making up the contract of December 13th, 1929?

A. Yes.

Q. And also the compilation of the figures showing [67] the payment to Mr. E. J. Lord as shown by the receipts which have been admitted in evidence?

A. Yes.

(Testimony of George Buchholtz.)

Q. And, with this end in mind, you consulted freely with Mr. E. C. Peters, the attorney for the company?

A. Yes.

Q. Did you have charge of making the book-keeping entries to carry out this transaction?

A. I did.

Q. You have just stated that at the close of each year the books of the company were balanced, but only considering the contracts of the company actually completed at that time?

A. That's right.

Q. And you had a profit and loss account, did you?

A. Yes.

Q. And after the profit or loss was determined at the end of the year what was done with the credit balance, if any, which appeared in the profit and loss account?

A. To surplus account.

Q. From what amount were the dividends of E. J. Lord, Limited, paid?

A. From the surplus account.

Q. Have you had photostatic copies made of the surplus account as shown in the books of E. J. Lord, Limited, and subsequently on the books of E. E. Black, Limited?

A. They were made by Judge Peters. [68]

(Testimony of George Buchholtz.)

Q. I call your attention to what purports to be photostatic copies of the surplus accounts. Have you seen these sheets before?

A. Yes.

Q. Are they photostatic copies of the surplus account of E. J. Lord, Limited, and subsequently E. E. Black, Limited?

A. They are.

Mr. WRENN: I offer these two sheets in evidence.

Mr. KAY: We have no objection, subject to a later check by Mr. Glass.

(Documents offered in evidence, consisting of two papers, received and marked, respectively: "Taxpayer's Exhibit 28A" and "Taxpayer's Exhibit 28B.")

Sheet No. 1.

TAXPAYER'S EXHIBIT 28-A

Account No.

Rating	Credit Limit			Name	SURPLUS ACCT.					
Business				Address						
Date	Items	Folio	✓	Debits	Balance	Credits	✓	Folio	Items	Date
1927										1926
					5,818.51	5,818.51		J61	By E. J. Lord	Dec. 31 1927
Dec. 31	To P. & L. (Dividends)	J50		50,000.00		5,512.57		J51	“ Profit & Loss 1/1/27	Dec. 31
“ “	“ Reserve for Taxes	J50		15,600.00		84,469.99		“	“ “ “ “ 12/31/27	“ “
“ “	“ Balance			30,201.07						
				<u>95,801.07</u>		<u>95,801.07</u>				
					30,201.07	<u>30,201.07</u>			By Balance	
Dec. 31	To Sundry Exp. deferred	(J50)		15,057.03						
“ “	“ Balance			15,144.04						
				<u>30,201.07</u>		<u>30,201.07</u>				1928
					15,144.04	<u>15,144.04</u>			By Balance	Jan. 1
Dec. 31	“ Dividends pd. 1928	J20		100,000.00		2,634.47		J23	“ Reserve for Taxes	Dec. 31
“ “	“ Goodwill	“		23,535.13		283,015.18		J23	“ Profit & Loss	“ “
“ “	“ Balance			177,258.56				“		“ “
				<u>300,793.69</u>		<u>300,793.69</u>				
1929					177,258.56	<u>177,258.56</u>			By Balance	1929
Mar. 31	To Dividends	J36		30,000.00	147,258.56	123,697.94		J138	“ Profit & Loss	Jan. 1
April 30	“ “	J48		50,000.00	97,258.56					Dec. 31
May 31	“ “	J64		70,000.00	27,258.56					
	“ Balance			152,956.50						
				<u>302,956.50</u>		<u>302,956.50</u>				
1929					(152,956.50)	152,956.50			By Balance	1929
Dec. 31	“Life Ins. Deposits	J134		4,776.00						Dec. 31
“ “	“ Balance			148,180.50						
				<u>152,956.50</u>		<u>152,956.50</u>				
1930					148,180.50	148,180.50			By Balance	1930
Aug. 31	To Dividends	J88		25,000.00	123,180.50					Jan. 1
Dec. 31	“ Balance			651,032.63		527,852.13		J145	“ Profit & Loss	Dec. 31
				<u>676,032.63</u>		<u>676,032.63</u>				

[Endorsed]: No. 2052. Filed February 1, 1932
at 11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court. [298]

(Testimony of George Buchholtz.)

Account No.....		TAXPAYER'S EXHIBIT 28-B				Sheet No.....				
Name		SURPLUS		Rating		Credit Limit				
Address				Business						
Date	Items	Folio	✓	Debits	Balance	Credits	✓	Folio	Items	Date
1931										1931
Febr. 28	To Treasury Stock	J16		476,074.00	651,032.63	651,032.63			By Balance	Jan. 1
					174,958.63					
					234,958.63	60,000.00		J41	Capital Stock	May 31
					241,534.79	6,576.16		J45	Treasury Stock	“ “

[Endorsed]: No. 2052. Filed February 1, 1932
at 11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court. [299]

(Testimony of George Buchholtz.)

Mr. WRENN: May I explain for the benefit of the Board that the same surplus accounts were kept during the time of E. J. Lord, Limited, and E. E. Black, Limited?

A. None of the books were changed at all.

Mr. WALSH: You asked him if these were the surplus accounts of E. J. Lord, Limited, and E. E. Black, Limited?

Mr. KAY: I said and subsequently of E. E. Black, Limited. One is the continuation of the other. The name was the only thing that was changed.

Mr. WALSH: That is a whole lot.

Mr. PETERS: It is the same corporation, but the name [69] is changed.

Q. Does this account show the condition of the surplus account of E. J. Lord, Limited, from the time of its incorporation down to until the time E. E. Black, Limited, finally redeemed the outstanding shares of stock formerly held by Mr. Lord?

A. It does.

Q. And does the credit balance from the profit and loss account which has been transferred to this surplus account carry the profits of this corporation from all sources?

A. It does.

Q. Are the profits of this corporation, referring to E. J. Lord, Limited, subsequently known as E. E. Black, Limited, as shown on these surplus accounts,

(Testimony of George Buchholtz.)

—were they returned in the income tax returns of the corporation for the respective years 1926 to 1930, both inclusive?

A. They were.

Q. The profits which you have transferred to this account from your profit and loss account, and returned in your income tax returns, are profits on which Territorial income taxes were paid for the calendar years 1926, 1928, 1929 and 1930?

A. That's right.

Q. At the time the first payment to Mr. E. J. Lord was made by E. E. Black, Limited, under the option dated December 13, 1929, did you open an account [70] for E. J. Lord?

A. Settlement account.

Q. This photostatic sheet I call your attention to is a photostatic copy of the account kept in the books?

A. Correct.

Mr. WRENN: We offer this photostatic copy of the ledger account, E. J. Lord settlement account, as an exhibit.

Mr. KAY: No objection subject to the condition that Mr. Glass may check.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 29.")

Sheet No.....
 Taxpayer's Exhibit 29
 Name E. J. LORD (Settlement a/c)
 Address
 Credit Limit
 Account No.....

Date	Items	Folio	Debits	Balance	Credits	Folio	Items	Date
1930			✓		✓			1930
Febr. 13	To Cash	C59	1,000.00		273,855.36	J5	By Treasury Stock-	Febr. 28
" 28	" Sundries	J4	249,000.00	23,855.36			Purch. a/c	
	Investments							
July 31	Bonds 23,000-							
" 17	Int. 482.36	J68	23,482.36					
	Cash 373.00	C99	373.00					
			<u>273,855.36</u>		<u>273,855.36</u>			
Dec. 26	" Cash	C137	68,313.98		175,313.98	J129	" "	Dec. 31
" 31	" Sundries	J128	108,277.86		1,277.86	J139	" Sundries	" "
			<u>176,591.84</u>		<u>176,591.84</u>			
				40% Tax %				
				26,904.66				1931
Mar. 13	To Cash	C163	6,726.17	20,178.49				Febr. 28
May 31	To Treasury Stock	J44	6,576.16	13,602.33				
June 15	" Cash	C181	6,726.17					

[Endorsed]: No. 2052. Filed February 1, 1932
 at 11:40 o'clock A. M. Robert Parker, Jr., Clerk
 Supreme Court. [300]

Q. At the time the first payment was made to Mr. E. J. Lord, February 30th, did you open an account known as "The Treasury account"?

A. "Treasury Stock Purchase Account."

Q. Is that the account in which you carried the stock of the corporation as redeemed from Mr. E. J. Lord?

A. Yes.

Q. This is a photostatic copy of the ledger account?

A. Correct.

Mr. WRENN: I offer in evidence photostatic copy of the Treasurer's stock purchase account.

Mr. KAY: Same understanding.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 30.") [71]

Testimony of George Buchholtz.)

Sheet No. 1.		TAXPAYER'S EXHIBIT 30				Account No.....	
Debiting Business		Credit Limit		Name Address		Treasury Stock Purchase Acct.	
Date	Items	Folio	Debits	Balance	Credits	Folio	Date
930							
Febr. 28	To E. J. Lord (Spec. a/c)	J4	273,855.36	273,855.36			
Dec. 31	" "	J128	175,313.98	449,169.34			
931							1931
Febr. 28	" (tax a/c)	J16	26,904.66	476,074.00	476,074.00	J17	By Surplus a/c
					476,074.00		
May 31	" Surplus	J44	6,576.16		6,576.16	J45	By E. J. L. Settlement Acct.)
							May 31

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 Supreme Court. [301]

(Testimony of George Buchholtz.)

Q. I call your attention to what purports to be a photostatic copy of the capital stock account. Is that a photostatic copy of the capital stock account on the ledger of the corporation?

A. Yes, sir.

Mr. WRENN: I offer in evidence capital stock account from the ledger,—photostatic copy of the same.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 31.")

(Testimony of George Buchholtz.)

Q. I call to your attention a group purporting to be photostatic copies of journal accounts. I will ask you if these are the photostatic copies of entries in the journal of the corporation showing the method by which the transaction between Mr. E. J. Lord and the corporation was carried on?

A. They are.

Q. And they are photostatic copies of the journal of the corporation?

A. Yes.

Q. And they carry the journal entries from February 28, 1930, the date of the first payment to Mr. Lord, down through May 31, 1931?

A. That's right.

Mr. WRENN: I offer the group of photostatic copies of the journal account as one exhibit.

(Documents offered in evidence, consisting of nine pages, received and marked: "Taxpayer's Exhibit 32.")* [72]

Q. From the books of the corporation have you prepared a statement showing an analysis of the money that was distributed to Mr. E. J. Lord out of the capital and surplus of the company?

A. I did.

Mr. WRENN: I offer statement showing analysis of the moneys paid to Mr. E. J. Lord as an exhibit.

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 33A" and "Taxpayer's Exhibit 33B," respectively.)

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 33 A - B

STATEMENT SHOWING ANALYSIS OF \$468,219.98 Distributed to E. J. LORD BY E. J. LORD LTD. OUT OF CAPITAL AND SURPLUS.

Surplus Balance 12/31/29, plus 1930 profits (excluding 1930 Dividends)	676,032.63
Less Net Amount of 1930 profit not subject to 60% apportionment (As Exhibit -A-) attached	35,380.17
	<hr/> 640,652.46 <hr/>
60% of above \$640,652.46 due E. J. Lord	384,391.48
Plus Allowance for miscellaneous Equipment Charged to Contract Expense	3,500.00
Plus Allowance of 40% of Income Tax (as per Agrmt)	20,328.50
	<hr/>
Portion of SURPLUS distributed to E. J. Lord	408,219.98
60% " Capital " " "	60,000.00
	<hr/>
TOTAL DISTRIBUTION TO E. J. LORD (re 600 shares)	<hr/> 468,219.98 <hr/>

[Endorsed]: No. 2052. Filed February 1, 1932 at
11:40 o'clock A. M. (Sgd.) Robert Parker, Jr.,
Clerk, Supreme Court. [303]

(Testimony of George Buchholtz.)

EXHIBIT "A"

1930 Profits NOT subject to 60% Apportionment		
Profit from Contracts:		38,225.61
Hawaiian Pine Job	12,107.13	
Nawiliwili Wharf Road	12,243.28	
Kapaa Swamp	6,299.95	
Rodger's Airport	5,609.05	
Sundry Contracts	1,966.20	
		<hr/>
Plus Sundries, (Interest, Plant Rental etc.)		57,027.44
		<hr/>
		95,253.05
Less Discount on Bonds	1,525.00	
" Expense Accounts	52,254.02	53,779.02
		<hr/>
		41,474.03
Less Portion of Tax reserve (Not		
Applicable to E. J. Lord)		6,048.81
		<hr/>
		35,425.22
Less Difference on Contracts per Auditor's Re-		
port of 7/31/30 as compared with books		45.05
St. Louis Heights, Naw. Wharf & Kapalama		
Wharf		
Auditor's Report	153,331.90	
As per Books	153,286.85	
		<hr/>
		45.05
		<hr/>
NET PROFITS FOR 1930 PER BOOKS		
(not participated in by E. L. Lord)		35,380.17

[304]

Q. I will ask you to examine Taxpayer's Exhibit 33A and 33B and tell us how much was actually paid to Mr. E. J. Lord in the matter of the redemption of these 600 shares of stock?

A. \$468,219.98.

(Testimony of George Buchholtz.)

Q. How much of that sum represents what was paid from the capital account?

A. Sixty thousand dollars.

Q. And sixty thousand dollars represents the original capital contribution at the time of the incorporation of E. J. Lord, Limited?

A. That's right.

Q. And the difference between the \$60,000. and \$468,219.98 is income taken from the surplus account?

A. Yes.

Q. Upon which a Territorial income tax has been paid by the corporation?

A. Yes. [73]

Q. And the difference between the sixty thousand dollars and the \$468,219.98 is \$408,219.98 paid out of the surplus account, upon which a Territorial income tax of two per cent. has been paid?

A. That is right.

Q. Were all the payments made to E. J. Lord made in cash?

A. No.

Q. How were some of the payments to him made?

A. Part of them in bonds.

Q. And when he was paid in bonds you figured the book value of the bonds as of the date of the payment?

A. No, at par value, which was agreed upon.

Q. It was agreed upon in your original agreement?

(Testimony of George Buchholtz.)

A. Yes.

Q. Also considering the accrued interest, if any, on the bonds?

A. Yes.

Q. Have you prepared any statement other than the receipts, which show when bonds were paid to Mr. E. J. Lord or do the receipts fully show that?

A. The receipts fully show that.

Q. Please examine Taxpayer's Exhibit 15 and 16. Do taxpayers' Exhibits 15 and 16 show the methods by which payment was made and in what specie payment was made to Mr. E. J. Lord?

A. Yes. [74]

Q. But, whether paid in cash or by bonds, the entire payment to him of \$408,219.98 was out of surplus, representing profits, upon which a Territorial income tax of two per cent. had been paid?

A. Yes.

Q. In figuring the amount due Mr. E. J. Lord on the redemption of the stock I note you have considered the income of E. E. Black, Limited, for the 12 months preceding January 1, 1931. Just how was it that the share of Mr. E. J. Lord under the agreement was figured in the income of E. E. Black, Limited, for the 12 months of 1930.

A. Mr. Lord was interested in a certain amount of contracts; in fact, five of them that were not completed until sometime in 1930.

Q. Have you made an analysis of those contracts?

A. I have.

(Testimony of George Buchholtz.)

Q. Is that Exhibit A, which is attached to Taxpayer's Exhibit 33?

A. Yes.

Q. And were all the contracts in which Mr. Lord was interested completed during the year 1930?

A. Yes, sir.

Q. Subsequent to the year 1930 was there an adjustment under the provisions of the agreement of December 13, 1929 made with Mr. Lord for the payment of the [75] Federal income tax?

A. I didn't understand the first part of the question, quite.

(Question read by the reporter.)

A. Yes, sir.

Q. How much was paid him for that purpose?

A. \$20,328.50.

Q. What does the item of \$3,500. represent in Taxpayer's Exhibit 33?

A. That was an agreement that was reached in connection with that difference on the valuation of their plant, and it was finally compromised to pay Mr. Lord \$3500. extra.

Q. Does that \$3500 that you have there represent profits of the corporation upon which a Territorial income tax of 2 per cent. had been paid?

A. Yes.

Mr. WALSH: What does this income tax of 2 per cent. represent? It is down here 5 per cent.

Mr. WRENN: What return are you referring to?

(Testimony of George Buchholtz.)

Mr. WALSH: All of them.

The WITNESS: Five per cent. is right.

Mr. KAY: One provision was amended and the other was not. The rate was amended to five, and I assume you are referring to that exception set forth.

Mr. PETERS: Just using the words of the Statute, the Statute itself was never expressly amended. [76] As long as you pay 2 per cent., if you pay three more, you are exempt.

Q. However, for the purpose of the record, for the years 1926 to 1930, both inclusive, the corporation income tax that was paid was five per cent.?

A. I think it was right along.

Q. Whatever the rate was that was paid, the profit and loss which is reflected in your surplus account paid the Territorial corporation income tax during all those years?

A. Yes.

Q. I call your attention to Taxpayer's Exhibit 30 showing the ledger account of Treasurer's,—treasury stock purchase account. Will you explain why it was you carried this treasury stock purchase account down to the time the stock was finally paid?

A. There was no ascertaining what amount would be paid; first of all on account of the uncompleted contracts, and, second, it could not be ascertained until the books were closed and the taxes were figured out.

(Testimony of George Buchholtz.)

Q. Until the stock had been fully redeemed by the corporation from Mr. E. J. Lord, you carried this entire transaction in a stock purchase account?

A. Yes.

Q. And as soon as it had been fully redeemed you applied to the Treasurer for a reduction of the capital stock?

A. Yes. [77]

Q. And prior to petitioning the Treasurer of the Territory of Hawaii for a reduction of the capital stock of the corporation from one hundred thousand to forty thousand dollars you had been advised by Mr. MacComisky and Mr. Camp there was no Territorial income taxes due, and the amount distributed to Mr. Lord?

A. Yes.

Q. I have asked you to examine a statement entitled: "E. J. Lord, Limited, statement of surplus account from September 1, 1926, the date of incorporation, to date of December 31, 1930, showing reconciliation with Territorial income tax returned and amount of corporation income tax assessed on the profits of the company." E. J. Lord, Limited, is a misnomer, is it not. It is now known as E. E. Black, Limited?

A. Yes, sir.

Q. Was this statement prepared by you and Mr. H. W. Camp?

A. It was.

Q. Does it reflect the condition of the surplus account of the corporation from 1926 to the end of 1930?

(Testimony of George Buchholtz.)

A. Yes, sir.

Q. And the amount of the balance in the surplus account, amount credited to surplus account in each of the years 1926, 1928, 1929 and 1930?

A. Yes.

Q. Does this statement show the amount of net taxable [78] income as shown on the Territorial income tax return for the 12 months preceding January 1, 1927 for the calendar years 1927, 1928, 1929 and 1930?

A. Yes, sir.

Mr. WRENN: I offer this sheet in evidence.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 34.")

TAXPAYER'S EXHIBIT 34
E. J. LORD, LIMITED

STATEMENT OF SURPLUS ACCOUNT FROM SEPTEMBER 1, 1926, THE DATE OF INCORPORATION, TO DECEMBER 31, 1930, SHOWING RECONCILEMENT WITH TERRITORIAL INCOME TAX RETURNS AND AMOUNT OF COR-PORATION INCOME TAX ASSESSED ON THE PROFITS OF THE COMPANY.

Line No.	Surplus at Sept. 1, 1926 Date of In-corp'n.	1926	1927	1928	1929	1930	Grand Totals
1.	Gross Income per Tax Return	\$16,966.10	\$1,111,352.11	\$340,102.48	\$220,504.13	\$681,509.48	\$2,370,434.30
2.	Total deductions per tax return	11,453.53	1,041,729.15	12,989.03	132,047.43	76,373.20	1,274,592.34
3.	Net taxable income	5,512.57	69,622.96	327,113.45	88,456.70	605,136.28	1,095,841.96
4.	Plus Non-taxable items						
	Reserve for taxes debits			12,965.53	57,077.16	20,000.00	90,042.69
	Bad Debts			23.50			23.50
	Int. on Exempt Bonds				1,865.62	4,607.59	6,473.21
5.	Total	5,512.57	69,622.96	340,102.48	147,399.48	629,743.87	1,192,381.36
	Less non-deductible items						
	Donations		210.00	63.80	325.00	275.00	873.80
	Reserve for taxes-credits			57,000.00	20,077.16	101,616.74	178,693.90
	Bad Debt			23.50			23.50
	Accrued Int. on bonds				1,299.38		1,299.38
6.	Net Profit per books	5,512.57	69,412.96	283,015.18	125,697.94	527,852.13	1,011,490.78
7.	Surplus Account						
	Add Credits—Cr. Bl. 1st of Yr.	5,818.51	11,331.08	15,144.04	177,258.56	148,180.50	5,818.51
	Profit—Line 6	5,512.57	69,412.96	283,015.18	125,697.94	527,852.13	1,011,490.78
	Reserve for taxes			2,634.47			2,634.47
8.	Deduct Debits	11,331.08	80,744.04	300,793.69	302,956.50	676,032.63	1,019,943.76
	Dividends Paid						
	Good Will						
	Reserve for taxes		50,000.00	100,000.00	150,000.00	25,000.00	325,000.00
	Adjust. Ins. Policy		15,600.00	23,535.13			23,535.13
9.	Balance Surplus Account				4,776.00		4,776.00
10.	Territorial Income Tax Assessed vs. Corporation 5% on line 3	11,331.08	15,144.04	177,258.56	148,180.50	651,032.63	651,032.63
		275.63	3,481.15	16,355.67	4,422.84	30,256.81	54,792.10
		275.63	3,481.15	16,355.67	4,422.84	30,256.81	54,792.10

[Endorsed]: No. 2052. Filed February 1, 1932

at 11:40 o'clock A. M. (Sgd.) Robert Parker, Jr.,
Clerk Supreme Court.

(Testimony of George Buchholtz.)

Q. I note that on March 12, 1931, there was filed with the Treasurer of the Territory of Hawaii an application to reduce the capital stock of E. E. Black, Limited, from \$100,000. to \$40,000. why was it that this application was not filed prior to this time?

A. It was done within less than a week's time after the books had been closed, and it had been ascertained the amount to be paid by Mr. Lord on account of taxes.

Q. In other words, you postponed this until the amount for the redemption of the stock had been paid?

A. It couldn't have been done before.

Q. I call your attention to the statement in regard to the redemption of the 600 shares of stock. You have examined that before?

A. Yes.

Q. It contains a resume of the journal entries of how this transaction was carried on to January 1, 1931? [79]

A. Yes.

Mr. WRENN: I offer this in evidence.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 35A and "Taxpayer's Exhibit 35B.")

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 35

E. J. LORD, LIMITED

JOURNAL ENTRIES RE REDEMPTION 600 SHARES STOCK

Date	Journal	Dr.	Cr.
Feb. 28, 1930	Treasury Stock—Purchase a/c	\$273,855.36	
	To E. J. Lord—Settlement a/c		\$273,855.36
Jr.-5	To set up, as of 1-1-30, the initial amount to be paid to Mr. E. J. Lord for his shares in terms of the agreement dated 12-13-29—i.e., 60% of the net worth of E. J. Lord, Ltd. as of 12-31-29.		
Feb. 28, 1930	E. J. Lord—Settlement a/c	249,000.00	
	to Notes Receivable		100,000.00
	Bonds		119,000.00
	Investments		30,000.00
Jr.-5	To record the transfer of the above stated assets to Mr. E. J. Lord's a/c, as a partial settlement of the amount payable at the termination of the option in terms of the agreement dated 12-13-29.		
July 31, 1930	E. J. Lord—Settlement a/c	23,482.36	
	to Bonds		23,000.00
Jr.-69	Expense Interest		482.36
	To charge former a/c as per agreement.		
Dec. 31, 1930	Treasury Stock—Purchase a/c	175,313.98	
	To E. J. Lord Settlement a/c		175,313.98
Jr.-129	Final payment for 600 shares of E. J. Lord Co. stock.		
Dec. 31, 1930	E. J. Lord—Settlement a/c	108,277.86	
	To Investments		39,000.00
Jr.-129	Bonds		68,000.00
	Interest on Bonds		607.50
	Expense Interest		670.36
Dec. 31, 1930	Expense Interest	670.36	
	Interest on Bonds	607.50	
Jr.-139	to E. J. Lord Settlement a/c		1,277.86
	Supplementary to final settlement.		
Feb. 28, 1931	Treasury Stock	26,904.66	
	To E. J. Lord—Tax a/c		26,904.66

(Testimony of George Buchholtz.)

Jr.-17	Being 40% of Lord's Inc. Taxes in connection with redemption of his 600 shares (as per agreement) payable when due.		
Feb. 28, 1931	Surplus	476,074.00	
	to Treasury Stock		476,074.00
	To close latter a/c on a/c of redemption of stock.		
			[306]
May 31, 1931	Capital Stock	60,000.00	
	to Surplus		60,000.00
Jr.-41	Reduction of Capital Stock by redemption of 600 shares, approved by Treas., Territory of Hawaii, May 29th as of Mar. 12th, 1931.		
May 31, 1931	E. J. Lord—Settlement a/c	6,576.16	
	to Treasury Stock		6,576.16
Jr.-45	Difference original 40% of return \$26,904.66 and corrected \$20,328.50.		
May 31, 1931	Treasury Stock	6,576.16	
	to Surplus		6,576.16
Jr.-45	To transfer former a/c		6,576.16

[Endorsed]: No. 2052. Filed February 1, 1932 at 11:40 o'clock A. M. (Sgd.) Robert Parker, Jr., Clerk Supreme Court. [307]

Q. You brought with you the minute book of the corporation?

A. Yes, sir.

Mr. WRENN: I find that all of these minutes have not been copied by my stenographer. I will offer all the minutes at the next session.

(Adjourned to 8:30 o'clock a.m., Saturday, December 5, 1931.) [80]

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Saturday, December 5, 1931, at 8:30 o'clock a.m., before

(Testimony of George Buchholtz.)

the aforesaid Board, all members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

Mr. WRENN: I would like at this time to make a part of the record a letter that I asked for and obtained from Dr. Nils P. Larsen this morning relative to the physical condition of Mr. E. J. Lord. We are not going to have him testify because of his physical condition. We had him examined yesterday by Dr. Larsen and this letter fully explains his condition.

Mr. KAY: No objection.

Mr. WRENN: May this letter be made part of the record.

(Letter from Dr. Nils P. Larsen, dated December 4, 1931, offered in evidence, received and marked: "Taxpayer's Exhibit 36.")* [81]

Mr. WRENN: At this time I offer in evidence as one exhibit the minutes of the meetings of the shareholders of E. J. Lord, Limited, February 15, 1930, February 28, 1930, and March 7, 1931. We have these in lieu of the originals. We have the originals here.

(Documents offered in evidence received and marked, respectively, "Taxpayer's Exhibit 37A," "Taxpayer's Exhibit 37B," and "Taxpayer's Exhibit 37C.")

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 37-A

SPECIAL MEETING OF STOCKHOLDERS OF
E. J. LORD, LIMITED.

Time: February 15th, 1930.

Place: The place of business of the company,
Pohukaina Street, Honolulu, T. H.

A special meeting of the stockholders of E. J. Lord, Limited was called to order by the President on February 15th, 1930 at 11 o'clock A. M. at the place of business of the Company, Pohukaina Street, Honolulu, T. H.

E. J. Lord, President, presiding.

The undersigned Secretary acting as secretary.

Upon roll call it was found that all of the members of the company were present personally and represented all of the outstanding shares of the stock of the company, to-wit, 400 shares, that is to say:

E. E. Black owning and representing 396 shares

E. J. Lord owning and representing 1 share

Geo. Buchholtz

owning and representing 1 share
(by proxy to Geo. Buchholtz

P. J. Erben (owning and representing 1 share

T. Ikejiri owning and representing 1 share

All of the members of the corporation there present thereupon signed the following written consent to said meeting:

We, the undersigned constituting all the members of E. J. Lord, Limited present at the meeting of which the within are minutes, consent to

(Testimony of George Buchholtz.)

this meeting and in token of said consent subscribe our names hereto.

(Sgd.) E. J. LORD

(Sgd.) E. E. BLACK

(Sgd.) GEO. BUCHHOLTZ

(Sgd.) P. J. ERBEN—by power of
attorney to Geo. Buchholtz

(Sgd.) T. IKEJIRI

No. 2052. Filed February 1, 1932 at 11:40 o'clock
A. M.

ROBERT PARKER, JR.,

Clerk Supreme Court. [308]

The following resolution was duly offered and
unanimously carried:

“RESOLVED by the stockholders of E. J. Lord, Limited that the Articles of Association of the corporation be amended so that the name of the corporation appear therein as ‘E. E. Black, Limited’ instead of ‘E. J. Lord, Limited,’ and that the title and Articles 1 and 8 respectively read as follows:

‘ARTICLES OF ASSOCIATION

—of—

E. E. BLACK, LIMITED’

‘1. The name of the company is and shall be
‘E. E. BLACK, LIMITED.’

‘8. The Company shall have succession and corporate existence for the term of fifty (50) years from the date of these presents and become a body corporate under the name and

(Testimony of George Buchholtz.)

style of 'E. E. Black, Limited,' and subject to all the liabilities provided by law for incorporated companies, and shall be subject to and have all the benefits of all general laws now and hereafter enacted in regard to corporations. All the property of the Company shall be liable for the just debts of the Company, but no shareholder shall be liable for the debts of the Company beyond the amount of what is due upon the share or shares owned by him.'

RESOLVED, FURTHER, that the proper officers of this company be, and they are hereby authorized and directed to make application to the Treasurer of the Territory of Hawaii in accordance with law for the allowance and confirmation of the amendments aforesaid and to make and file all such affidavits and other instruments as may be necessary or proper to effectuate the purpose, intent and direction of this resolution."

There being no further business, upon motion duly made and carried, the meeting adjourned.

(Sgd.) T. IKEJIRI,

Secretary. [309]

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 37B

MINUTES of the annual Meeting of Shareholders of E. E. Black, Ltd., held at the office of the Company in Honolulu on February 28th, 1930 at 3 P. M.

PRESENT:

Mr. E. E. Black	(owning 400 shares)
“ Geo. Buchholtz	(by invitation)
“ T. Ikejiri	(“ “)

All outstanding Shares being represented, the meeting came to order.

MINUTES of February 15th, 1930.

The Minutes of the Special Meeting of February 15th, 1930 were read, and approved as read.

AMENDMENT OF ARTICLES OF ASSOCIATION:

E. E. Black stated that the amendment to the Articles of Association had been amended to change the name of the Company to E. E. Black, Limited, and had been granted and approved by the Governor of the Territory of Hawaii, and directed that a copy of the Amendment be affixed in the Minute book.

ELECTION OF DIRECTORS AND AUDITORS:

Mr. Black moved that the following be elected as Directors:

“ Frank Jose

and Messrs. Young, Lambertson & Pearson as auditors.

ADJOURNMENT:

There being no further business the meeting adjourned.

(Sgd.) T. IKEJIRI. [310]

TAXPAYER'S EXHIBIT 37-C

MINUTES of the annual Meeting of Stockholders' of E. E. Black, Ltd., held at the office of the Company on March 7th, 1931 at 9:30 A. M.

PRESENT:

E. E. Black, Ltd.) “ 600 “

MINUTES of February 28th, 1930:

The Minutes of the Meeting of Stockholders of February 28, 1930 were read, and approved as read.

(Testimony of George Buchholtz.)

AUDITOR'S REPORT:

The Auditor's report dated March 3rd, 1931 was submitted and read, including Auditor's Certificate and Balance Sheet as of December 31, 1930.

Mr. Black moved that the Auditor's Report be approved and filed in the Minute Book as part of the Minutes.

ELECTION OF OFFICERS:

Mr. Buchholtz nominated the following directors, there being no further nomination, the Secretary was asked to cast the ballot.

Mr. E. E. Black

Mr. P. J. Erben

Mr. Geo. Buchholtz

Mr. T. Ikejiri

Mr. R. J. Davis

carried unanimously.

ELECTION OF AUDITOR:

Mr. Black moved that Messrs. Young, Lambertson & Pearson be re-elected.

Mr. Buchholtz seconded the motion, carried unanimously.

REDUCTION OF CAPITAL STOCK:

Mr. Black moved that the following resolution be passed:

"WHEREAS E. E. Black, Ltd. has an authorized Capital [311] Stock of \$100,000. divided into 1,000 shares of the par value of \$100. each and has purchased from one of its

(Testimony of George Buchholtz.)

stockholders 600 of said shares of the par value of \$100. each, of the aggregate par value of \$60,000.—, and has paid for the same and holds the same in its treasury and desires to retire said 600 shares and reduce its capital stock accordingly to \$40,000.—divided into 400 shares of the par value of 100 each,

THEREFORE BE IT RESOLVED that the authorized capital stock of E. E. Black, Ltd., be reduced from \$100,000.—divided into 1,000 shares of the par value of \$100.—each to \$40,000.—divided into 400 shares of the par value of \$100.—each by retiring 600 shares of the par value of \$100.—each now held in the treasury;

That a sworn certificate signed by the presiding officer and secretary of this meeting be presented to the Treasurer of the Territory of Hawaii setting forth therein the action taken and certifying that at the time the vote on this resolution was taken the corporation was not and has not since become indebted in any manner over and above half of the amount of its remaining capital stock;

AND BE IT FURTHER RESOLVED that when the said reduction of capital stock is effected as required by law, the Treasurer of this corporation do retire and cancel the said 600 shares of the par value of \$100. each of this corporation now held in the Treasury.”

(Testimony of George Buchholtz.)

Mr. Buchholtz seconded the motion, carried unanimously.

There being no further business, the meeting adjourned.

[Seal]

(Sgd.) T. IKEJIRI,
Secretary. [312]

Mr. WRENN: I offer in evidence at this time as one exhibit minutes of the Board of Directors of E. J. Lord, Limited, dated December 7, 1929, February 28, 1930 and December 20, 1930.

(Documents offered in evidence received and marked, respectively, "Taxpayer's Exhibit 38A," "Taxpayer's Exhibit 38B," and "Taxpayer's Exhibit 38C.")

TAXPAYER'S EXHIBIT 38-A

MINUTES of a Special Meeting of the Board of Directors of E. J. Lord, Ltd., held at the office of the Company in Honolulu, T. H., on December 7th, 1929 at 10 A. M.

PRESENT:

Mr. E. E. Black

Mr. Geo. Buchholtz

Mr. T. Ikejiri

CHAIRMAN:

Mr. E. E. Black, Vice-President of the Company, took the Chair and called the meeting to order.

(Testimony of George Buchholtz.)

MINUTES OF MAY 31st:

The minutes of the meeting of May 31st were read, approved, and ordered placed on file.

PURCHASE OF STOCK:

Mr. E. E. Black moved that as Mr. E. J. Lord was willing to sell all his stock of E. J. Lord, Ltd. the Company was to redeem the 600 shares for which the Company was to pay for the said shares in the following manner:

(1) The sum of money equal to 60% of the net worth of the Company as of December 31st, 1929.

(2) The sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929.

(3) The sum of money equal to 40% of the amount to which Mr. E. J. Lord may become liable for Federal and Territorial Income Taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares.

Mr. Lord agreed to give the Company an option to purchase the above mentioned stock to February 28th, 1930, and to have an agreement drawn signed by both parties covering the above option, price and payments to be made, a copy of such agreement to be entered into the Minute-book. Mr. Geo. Buchholtz seconded the motion which was carried unanimously.

Mr. Buchholtz moved that the Company upon the exercise of the option cause its articles of

(Testimony of George Buchholtz.)

Association to be amended so that the name does not contain the name "E. J. Lord" or any words similar to said name. [314]

Mr. Black seconded the motion to be carried unanimously.

ADJOURNMENT:

There being no further business, the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary.

[Endorsed]: No. 2052. Filed February 1, 1932 at 11:40 o'clock A. M. Robert Parker, Jr., Clerk, Supreme Court. [315]

TAXPAYER'S EXHIBIT 38-B

Meeting of Directors of E. E. Black, Ltd., held in Honolulu, February 28th, 1930 at 3:15 p.m.

PRESENT:

Mr. E. E. Black
" Geo. Buchholtz
" T. Ikejiri
" R. J. Davis
" Frank Jose

CHAIRMAN:

Mr. Black took the chair and called the meeting to order. The Chairman stated that a majority of the Directors were present and met by consent.

(Testimony of George Buchholtz.)

ELECTION OF OFFICERS:

Mr. Black moved that the following officers be elected, seconded by Mr. Buchholtz and carried unanimously.

Mr. E. E. Black, President

“ P. J. Erben, Vice-President

“ Geo. Buchholtz, Treasurer

“ T. Ikejiri, Secretary

AUDITORS REPORT:

The Auditors Report dated January 29th, 1930, with Balance Sheet as of 12-31-1929 was submitted and read. Mr. Ikejiri made the motion, and seconded by Mr. Black that the Auditor's Report be approved and placed on file in the minute book.

TREASURY STOCK:

Mr. Buchholtz stated that Mr. E. J. Lord had turned in his 600 shares on February 15th, 1930, and had been paid \$250,000.00 on account, with interest from January 1st, 1930 to February 15th, 1930, as per agreement.

ADJOURNMENT:

There being no further business the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary. [316]

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 38-C

MINUTES of a Special Meeting of the Board of Directors of E. E. Black, Ltd. held at its office on December 20th, 1930 at 10 A. M.

PRESENT:

Mr. E. E. Black, President
“ Geo. Buchholtz, Treasurer
“ T. Ikejiri, Secretary

CHAIRMAN:

Mr. Black took the chair, there being a quorum present, called the meeting to order.

MINUTES of December 5th, 1930:

The minutes of the special meeting of December 5th, 1930 were read, approved and ordered placed on file.

MR. FRANK JOSE REMOVED AS DIRECTOR:

Mr. Ikejiro moved that whereas Mr. Frank Jose was no longer in the employ of the Company, he be removed as a Director, Mr. Black seconded the motion, carried unanimously.

FINAL SETTLEMENT WITH MR. E. J. LORD:

Mr. Buchholtz read the Auditor's Report to July 31st, 1930 as well as Mr. MacComiskey's letter re. Taxes, dated December 17th, 1930, as well as a yet unmailed letter to Mr. Lord of December 19th, 1930, showing that Mr. Lord's share in the final settlement from the above reports came to \$170,536.12 with additional

(Testimony of George Buchholtz.)

\$3,500.00 for Plant, as agreed in meeting of December 5th, 1930, making a total of \$174,-036.12.

Mr. Ikejiri moved that the above mentioned letter be mailed to Mr. Lord, and that copies of the mentioned reports and letters be placed in the Minute book, and that the treasurer be directed to pay to Mr. Lord the sum of \$174,-036.12 in Bonds and Cash, as set forth in letter to Mr. Lord, dated December 19th, 1930, and receive from Mr. Lord therefor a receipt in full settlement, with the proviso, that the 40% of Federal and Territorial Income Taxes, to which Mr. Lord becomes liable upon income accrued by reason resulting from the sale of the 600 shares of E. J. Lord, Ltd., will be paid upon assessment, as per agreement of December 13th, 1929.

BONUS TO MR. BLACK:

The Treasurer stated that the financial condition of the Company, after having settled with Mr. E. J. Lord, was very sound, and stated that the Profits on the Completed Contracts to November 30th, 1930 were \$620,612.35, less proportion of Operating Expenses of \$35,081.10, leaving a Net Profit on the above mentioned Contracts of \$585,531.25.

Mr. Buchholtz moved that Mr. Black be paid a Bonus of two per cent on the above mentioned Net Profit of \$585,531.25, making a sum of

(Testimony of George Buchholtz.)

\$11,710.60. Mr. Ikejiri seconded the motion, carried unanimously. Mr. Black directed the treasurer to pay the above amount.

ADJOURNMENT:

There being no further business, the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary. [317]

Mr. WRENN: With the consent of the attorneys for the Government we would like to have the appeal amended by inserting the words "E. J. Lord" after the word "Taxpayer" on the last line of page 2 of the appeal.

Mr. PETERS: Do you consent that the word be written in by the Board?

Mr. KAY: Yes. I have no objection.

H. W. CAMP

was duly called and sworn as a witness for the Taxpayer, and testified as follows: [82]

Direct Examination by Heaton L. Wrenn, Esq.

Q. Will you state your name, please.

A. H. W. Camp.

Q. You are assistant secretary of Hawaiian Trust Company, Limited?

A. I am.

(Testimony of H. W. Camp.)

Q. And is Hawaiian Trust Company, Limited, the agent for Mr. E. J. Lord?

A. It is.

Q. And as agent for Mr. E. J. Lord did you prepare his tax return for the 12 months preceding January 1, 1930?

A. I did.

Q. And that return was filed within the time prescribed by law?

A. It was.

Q. I call your attention to the original returns. Prior to making this return did you examine the surplus account of the corporation which is now known as E. E. Black, Limited?

A. Yes.

Q. And with reference to the surplus account did you also examine the profit and loss account of that corporation?

A. I did.

Q. What was the cost of Mr. Lord's stock in the corporation,—sixty thousand dollars?

A. That was the cost that I returned. [83]

Q. And you show that in the return, do you?

A. Yes.

Q. You have examined the assessment that was made by the tax assessor in this matter?

A. I have.

Q. And the assessment that was made by the tax assessor after the filing of the original return and after the filing of the amended return also allows

(Testimony of H. W. Camp.)

this sixty thousand dollars as the cost of the stock?

A. It does.

Q. Did you make a computation to determine how much was received by Mr. Lord from the corporation pursuant to the agreement of December 13, 1929, over and above his original capital contribution of sixty thousand dollars?

A. Yes.

Q. Is that computation a computation that was made by you,—is that attached to the return?

A. Yes, that has been furnished to the tax office.

Q. You likewise made a supplemental return, did you not?

A. I did.

Q. In making this computation did you prepare an analysis, working in conjunction with Mr. Buchholtz, of the surplus account of the corporation?

A. Yes.

Q. The difference between the total amount of \$468,000., in round figures, so received from the [84] corporation by Mr. Lord, and the sixty thousand dollars representing his original contribution, came entirely from the surplus account, did it not?

A. It did.

Q. Can you say from your analysis of the surplus account as to whether this is from the profits of the corporation, this difference?

A. Yes, the profits were transferred out of the profit and loss account to the surplus account.

(Testimony of H. W. Camp.)

Q. So the figure of \$406,569.98 which you have set forth in your supplemental return and schedule attached thereto represent profits of the corporation which were taken out of the surplus account and distributed to Mr. Lord?

A. That is correct, and the total account distributed there was \$1,650. in excess of \$406,569.98, that being due to certain attorney's fees which were considered as an expense to Mr. Lord on his tax return.

Q. And that expense was allowed by the assessor in making his assessment, was it not?

A. It was.

Q. And the \$406,000. plus the \$1650. making \$408,000. in round figures, came entirely from the surplus account and was paid out of profits?

A. It did.

Q. In connection with your analysis of the surplus account you examined the tax returns of E. J. Lord, [85] Limited, for the 12 months preceding January 1, 1927, and for the taxation years 1927, 1928 and 1929, as well as the return for the 12 months preceding January 1, 1931, of E. E. Black, Limited?

A. Yes, sir.

Q. And from your examination of these returns and from your analysis of the reports could you testify whether or no the corporation paid a corporation Territorial income tax upon this income which was distributed to Mr. Lord out of the surplus account?

(Testimony of H. W. Camp.)

A. Yes, that is correct.

Q. A Territorial income tax was paid on that?

A. It was.

Q. Yesterday Mr. Buchholtz, when he was testifying, identified an analysis of the surplus account of the corporation, which is Taxpayer's Exhibit 34, and stated that this was prepared by you in conjunction with him,—that is correct?

A. Yes, that is correct.

Q. What does Taxpayer's Exhibit 34 purport to show?

A. That exhibit was prepared in order to show that the corporation has paid an income tax on all of the profits with the exception, of course, of minor non-taxable and non-deductible items of the surplus.

Mr. PETERS: Non-taxable and deductible.

A. Non-taxable and non-deductible items,—showing that the company has paid an income tax on all of [86] that surplus with those exceptions, which has been paid over to Mr. Lord in settlement for the retired stock.

Q. In making this return you had access to the books of the corporation for the years involved?

A. Yes, and the office copies.

Q. And it is a photostatic copy of this that is now in evidence?

A. That is correct.

Mr. ADAMS: When you say "non deductible" you mean non-deductible from what?

(Testimony of H. W. Camp.)

A. Non-deductible from gross income.

Mr. ADAMS: If non-deductible it would be taxable, would it not?

A. Well, this schedule starts out with the gross income, as shown by the tax returns, and is adjusted from the non-taxable items and the non-deductible items under the Territorial law, resolving down to an agreement with the surplus account in the corporation accounts.

Mr. ADAMS: The non-deductible amounts being the amounts on which taxes are imposed?

A. That's correct.

Q. The dividend that was paid to Mr. Lord for his stock came out of this surplus account that you analyzed?

A. Yes, that's correct.

(Recess) [87]

Q. How long have you been connected with the Hawaiian Trust Company, Limited?

A. About 11 years.

Q. And during those entire eleven years what has been the nature of your work with the Hawaiian Trust Company?

A. My duties have been accounting and tax work,—tax accounting and also straight accounting.

Q. You are head of the tax department, are you not?

A. I am.

Q. And prior to going with the Hawaiian Trust Company in the year 1920 what experience, if any, did you have as an accountant?

(Testimony of H. W. Camp.)

A. I was connected with the firm then known as the Audit Company of Hawaii, now known as Young, Lambertson & Pearson, quite a number of years; about seven or eight years.

Q. What were your duties when you were connected with the Audit Company of Hawaii?

A. Duties of an auditor, senior auditor.

Q. In the event that E. H. Lord had declared a dividend, out of what account would it have declared this dividend?

A. It could only declare it out of surplus account, because all the profits of the company are transferred, under their bookkeeping system, to that account.

Q. And a dividend, if it had been declared, would have been charged against the surplus account?

A. It would have had to be so charged. [88]

Q. In the event that the corporation had declared a dividend of all its undivided profits in the surplus account what would have been the amount of that dividend at the end of 1929?

A. At the end of 1929 the surplus account showed a balance of \$148,180.50. If they had declared a dividend of the entire surplus account that would have been the amount.

Q. In addition to dividends charged against that account in the years 1927, 1928 and 1929—

A. There was no dividend in 1926. In 1927, 1928 and 1929 the dividends were charged to that ac-

(Testimony of H. W. Camp.)

count. I don't quite understand that last question. Will you state that again.

Q. This one hundred and five thousand dollars balance, in round figures, that you have testified to, would have been paid out of the surplus account in addition to the dividends which had already been declared in the previous years?

A. Yes, that is correct. There was a balance of \$148,000. roughly after paying of the dividends. Mr. Wrenn spoke of \$105,000. That amount, I believe, was \$148,000., the balance of surplus at the end of 1929.

Q. Of the \$468,000., in round figures, that was paid to Mr. E. J. Lord, sixty thousand dollars of that was declared out of the capital, was it not?

A. That is correct. [89]

Q. And the balance paid to him as a dividend of \$408,000. came out of surplus?

A. Yes.

Mr. ADAMS. May I ask a question? That surplus account of \$400,000. was earned profits?

A. Yes, the books of the company so reflect all of these items, with the exception of a small balance at the beginning of the surplus account, \$5,818.51. I didn't go into that figure. It may be earned profits, but all of the rest of the balance of that account is earned profits according to my analysis of the company's books.

Q. You have just stated that the balance in the surplus account at the close of 1929 was \$148,180.50.

(Testimony of H. W. Camp.)

Where did the balance of the \$408,000., in round figures, come from that was paid to him?

A. That balance was made up of additional profits on certain contracts completed in 1930, which were still pending and not taken into the surplus account at the end of 1929.

Q. And those profits from the uncompleted contracts were shown in the surplus accounts for the year 1930?

A. They were.

Cross Examination by Harold T. Kay, Esq.

Q. How long have you been acting as financial agent or otherwise for Mr. Lord?

A. I think our first duties in connection with Mr. [90] Lord's account started sometime in 1929, —at the close of 1929.

Q. At that time was Mr. Lord contemplating severing his connection with E. J. Lord, Limited?

A. That is something I cannot state. I don't know.

Q. Did he confer with you concerning the sale of his stock of E. J. Lord, Limited?

A. No, I didn't handle Mr. Lord's personal affairs in our office; merely his tax affairs. Those affairs are handled by other officers of the Trust Company.

Q. You made out the tax returns for Mr. Lord in 1929?

A. Not in 1929.

Q. 1930?

(Testimony of H. W. Camp.)

A. In 1931, based upon 1930 income.

Q. When did you have occasion to examine the books of E. J. Lord, Limited?

A. In connection with the preparation of Mr. Lord's returns in 1931.

Q. You made a complete examination of all the E. J. Lord, Limited books, did you?

A. Only of the surplus account.

Q. You had no occasion to examine the complete records of that company?

A. No, I made no complete audit. The books are audited by Young, Lamberton & Pearson. There was no necessity of my doing that.

Q. Do the books reflect the consideration that E. J. [91] Lord paid to E. J. Lord, Limited, for his 800 shares of stock issued to him in 1926?

A. My understanding is they do. I haven't examined the entries. I asked Mr. Buchholtz to inform me as to what had been paid in order to estimate the cost basis, and he gave me that information.

Q. What did the books show as the consideration paid by E. J. Lord for these 600 shares of stock sold by E. J. Lord?

A. They reflect the amount of \$468,000.

Q. That was the total consideration paid, was it?

A. I think so. That is shown in the settlement account which has already been filed as an exhibit and copy given to you.

(Testimony of H. W. Camp.)

Q. Do the books reflect a sale of that stock to the corporation for which the corporation pays the \$468,000?

A. The books do not mention a sale, as I recall it. They show that the stock was acquired from Mr. Lord and placed in their treasury account and subsequently that stock was redeemed.

Q. The books reflect that the corporation paid this \$468,000., do they not?

A. Yes, that was paid in cash and other assets.

Q. That was paid for the surrender of this 600 shares of stock by Mr. Lord?

A. That is correct, yes.

Q. What was the total amount of dividends paid by [92] E. J. Lord, Limited, as reflected by its books, in the year 1929?

A. \$150,000.

Q. In the year 1930?

A. \$25,000.

Q. In the year 1929 the books reflect a salary paid to E. J. Lord also, do they not?

A. I don't know.

Q. So that in the year 1930 the books reflect no dividends paid the stockholders other than the dividends of \$25,000?

A. I would not say that. There was a regular dividend paid out of the earnings of the company subsequent to the distribution from the surplus account to Mr. Lord in settlement for his stock. Mr. Lord did not participate, as I understand it, in the

(Testimony of H. W. Camp.)

ordinary dividends of \$25,000., those having been paid out of the profits after he received his distribution of the profits.

Q. Was there any distribution of capital or surplus, whichever name the cash resources of the company went under, to any of the other stockholders besides Mr. Lord?

A. No.

Q. Have you examined the minutes of the corporation?

A. To some extent.

Q. They reflect, do they not, that this amount of \$468,000. was paid to Mr. Lord in consideration of [93] his selling to the corporation his 600 shares of stock?

A. The minutes I saw refer to the settlement, the consideration that was paid to Mr. Lord as being a redemption of his stock.

Q. What was the reason for that redemption as reflected by the books?

A. You mean the account books or the minute books?

Q. Any records?

A. The accounting books do not show any reason for the corporation's redeeming Mr. Lord's shares and I do not recall seeing any definite reason in the minutes, excepting that the corporation wished to redeem these shares.

Q. You testified here you have been engaged in tax work for a long time and that you are now tax expert with the Hawaiian Trust Company?

(Testimony of H. W. Camp.)

A. Yes.

Q. The Territorial income tax imposes a tax on capital gains, does it not?

A. It does on the sale of assets.

Q. Assuming this situation, Mr. Camp,—Assume a stockholder owns 100 shares in Ewa Plantation and I sell or I buy those shares at \$35.; subsequently I sell those shares at \$40.,—the difference between the purchase price and the selling price constitutes a net capital gain to me, and on which I have to pay a Territorial income tax, does it not?

[94]

A. Yes.

Q. Now in Section 1391 the exemption stated by the Statute is directed to dividends paid on stock owned, is it not?

A. Section 1308, I believe, covers exemption of dividends.

Q. Referring you to Section 1391, the last proviso thereof, will you state whether or not that proviso provides “That in assessing the income of any person or corporation there shall not be included the amounts received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has been assessed upon the net profits of such corporation”?

A. That provision so states, yes.

Q. This distribution to Mr. Lord was not in the nature of a duly declared dividend distributable to all the shareholders from net profits, was it?

(Testimony of H. W. Camp.)

A. It was not the same as a regular dividend paid out of earnings, paid to all stockholders, but I consider it was a dividend paid out of the profits of the company.

Q. You considered it a dividend and not a gain on capital?

A. Yes, that is what I judged it to be.

Q. You have stated you make out the income tax returns for E. J. Lord, have you not?

A. Yes. [95]

Q. Will you state whether or not the document I hand you is a true copy of the Federal income tax return made out by you for E. J. Lord for the year 1930?

Mr. WRENN. I object to any examination on the Federal income tax return because the Federal income tax laws provide that upon liquidation any gains that may be received by the taxpayer is taxable as a capital gain. It cannot have any bearing on this controversy existing under our Territorial income tax laws.

Mr. KAY. May it please the Board, I will show the relevancy of this examination as we proceed.

Mr. ADAMS: Would you mind telling us what relevancy this has, in your opinion?

Mr. KAY: I think it will develop, may it please the Court. It has a clear relevancy or I would not be offering it,—clearly material, and I can see no legitimate grounds for an objection to it.

Mr. WRENN: I think the legitimate ground for objection to it is that we are not concerned with

(Testimony of H. W. Camp.)

the Federal income tax laws, and this is a return for the Federal income tax law which is mandatory and upon which a tax has been paid. If it has any relevancy, I think we are entitled to know it at this time.

Mr. ADAMS: I think so too. What is the relevancy?

Mr. KAY: The relevancy is simply this: The contention [96] of this witness is that this distribution was a dividend and it was not a capital net gain. In the Federal income tax return made out by this witness for the taxpayer under Schedule "D" capital net gain from sale or loss from sale of assets, you have more than two years. There is listed 600 shares E. J. Lord, Limited, 1926 to 1930, that is the date acquired and date sold, \$599,743.20 as the amount realized from the sale of his capital assets. The cost and value as of March, 1931, sixty thousand dollars; subsequent improvements and capital deductions, \$1,650.; net gain or loss, 12½ per cent., \$538,093.20. Upon cross examination we certainly have the right to acquire into the evidence already adduced in respect to this witness, the authenticity of that evidence; whether or not the position assumed by the taxpayer in this case is consistent with the position assumed in respect to other matters, and also whether the amount of gain is the same in both cases. Counsel says that the Federal law is different from our law. Under the Federal law, may it please the Court, when stock

(Testimony of H. W. Camp.)

is sold to a corporation, being the corporation's own stock, a tax is imposed and it is recognized that under the income tax, properly speaking, a tax is assessable. That tax may be either upon the net gain as a liquidating dividend or upon the net gain from the sale of capital assets. If it is plain [97] there is a sale of capital assets, which is binding of course upon the Taxpayer when so claimed, the rate is only $12\frac{1}{2}$ per cent. Where there is a liquidating dividend, as that is called, upon dissolution or otherwise, there is a surtax, and where the amount runs into large figures the sur-tax may be considerably in excess of the $12\frac{1}{2}$ per cent. Now the taxpayer in this case has considered this sale of his stock as a sale of capital assets and he has made that representation to the Federal government, and it will be noted that the amount he enters up as a sale of capital assets is greater than in the case at bar. Now, under our law, as Mr. Camp has stated, a tax is imposable and assessable upon profits derived from the sale of capital assets, and in this case our contention is that this clearly is out and out a sale of capital assets; that the two parties in this controversy, to-wit, E. J. Lord, Limited and E. J. Lord, are two distinct entities. The law so recognizes them. You can tax the stock, you can tax the corporation. The stockholder has no tenable interest in the property of the corporation. He simply owns that stock, which represents an interest which may mature upon dissolution. But here we have a con-

(Testimony of H. W. Camp.)

tinuing corporation; the stockholder sells his stock to the corporation for a consideration; he makes a profit, [98] the difference between the amount paid by the corporation and the amount that he paid the corporation for the stock. So we say that under any view of the case the contention of the taxpayer here, to-wit, that this is simply a dividend that has already born its tax, is without bottom and has no merit in it, and, in corroboration of that, along with other facts which we intend to prove, we bring the Federal income tax return and we show there the position adopted by the taxpayer in respect to this particular transaction. That position has been a sale of capital assets and so considered by him.

Mr. WRENN: I do not think this Board wants to open up the field of Federal income tax law. If you wish to go into that field, we are perfectly willing to do that, but it is incompetent, irrelevant and immaterial. Mr. Kay says that the liquidating dividend under the Federal law is not taxed as a capital gain. The Federal tax law says liquidating income shall be taxed as a gain. We are not going to get any place in the ultimate issue here by delving into the Federal income tax laws and Federal income tax return, and that is why I object to going off on this tangent.

Mr. PETERS: May I say a word. I think from the standpoint of the Territory the question directed to the Board is whether or not the evidence of this witness [99] should be considered at its face value

(Testimony of H. W. Camp.)

by reason of the fact that he has treated the same subject matter in a different way on another occasion, which if properly done is in direct conflict with what he contends here. I just want to say this, that as far as this particular question is concerned, if the Federal tax law requires expressly that certain income on certain transactions be treated in a certain way, you must treat them in that way. That is all there is about it. For instance, the United States has provided relative to the question of capital gains, the valuation as it existed on the 1st of March, 1913, and on that basis the United States returns are computed. Our local statute provides another method of computing income. Now, the situation is that as far as the Federal law is concerned it has suffered four amendments in regard to treating these liquidating dividends, and in 1926 it amended the law so that it definitely required, it became mandatory that as far as these liquidating dividends are concerned they should be returned in a certain way. Now, if the question that Mr. Kay now propounds is directed to the attention of the Board for a showing that under identically similar circumstances and an identically similar law this witness made an entirely different analysis of the situation and returned it differently, that is one thing. [100] Then we have the prior contradictory statement made under identical similar circumstances. But that is not the situation here. Counsel cites a Federal statute. Before this Board can come to the con-

(Testimony of H. W. Camp.)

clusion that this witness has made a prior contradictory statement in regard to the same matter, it must find the major premises, that all the facts and circumstances are the same; otherwise it is not a contradictory statement. If we get into this 1926 amendment, then we must go back to the entire history of the law. This Board will be called upon, not alone to determine the legal phases of our Territorial law, but it will be called upon to determine the legal phases of our Federal law, and determine whether or not the Federal law is the same as our Territorial law, otherwise it would not be a contradictory statement and different treatment of the same subject matter. Mr. Kay's contention would not only bring the Board into a consideration of the very issue involved in this appeal, but, as an ancillary matter, it would call upon the Board to decide what the Federal law means, too. So you have not only the problem to determine what the local law means, but you have to determine what the Federal law means, and see if the Federal law contains a provision to meet this identical provision. We haven't anything in the local law relative to liquidating dividends. [101] We are applying section 1391 in the spirit of the law. That, as far as the individual is concerned, after he receives a dividend, he shall not again pay a tax on that dividend where the corporation has already paid it. When anything comes to the stockholder as his dividend, you cannot call it any other name. Whether it has

(Testimony of H. W. Camp.)

the direct authorization of the two people that own the corporation, to-wit, Lord and Black, it is a dividend, if the Board please, by whatever name you call it. To ask this witness why under these circumstances he made this particular return as to the Federal law in one way, and then returned it in respect to the Territorial law in another way, unless the laws are the same, unless the provisions are the same, we cannot consider it. We all know the arbitrary rules that have been fastened on us by the Federal law in regard to our income. In many instances there is neither rhyme nor reason in it, but we have to do it because they require it in a particular way. If we go into this entire proposition as counsel would like to have us go into it, we not alone have to go into the 1926 amendment, but we have to go into the 1917 amendment and the 1921 amendment and the relation that the three amendments, 1923, 1917 and 1926 bear to the original act of 1913, and every phase of the treatment of liquidating dividends by the United States will [102] have to be examined. I don't object, and, as far as we are concerned, we will welcome the opportunity to examine the Federal law and see how the Federal law has treated this particular subject,—not alone under the 1926 law, where the exact transaction has been taken up and disposed of by reason of the fact that the earlier amendments contained no reference to it. We welcome that. We welcome all the information the Board can get on this sub-

(Testimony of H. W. Camp.)

ject as to the Federal law or any other tax law. I do not care to have the record show here, or have the record encumbered with the attempt to show that Mr. Camp, after a study of the facts and circumstances of this particular case, has acted in respect to the same law differently.

Mr. ADAMS: Your contention is that what goes under the Territorial laws as liquidating dividend under the Federal law of 1926 must be classed as a capital account and therefore goes back to the value of that capital in 1913?

Mr. PETERS: Yes, so it has no application to the Territorial law whatever.

Mr. KAY: It seems as if we are getting the cart before the horse in this matter. My question was directed as to whether or not this return was a true copy. Lets find out wherein the Federal law differs from our law. Let's find out whether this return is based upon an entirely different law and [103] that facts stated in respect to that law are not applicable to our own law. The question of capital is a fact, not a question of law. It is a fact, and where representation is made of a certain transaction which results in a capital account, that is a fact. Our law taxes capital accounts. The Federal law, as you gentlemen are well aware, is apparently an out and out income tax law. Our law was modeled on the Federal law. The Legislature has from time to time directed that our administration officials follow as nearly as possible Federal adminis-

(Testimony of H. W. Camp.)

tration. In the case at bar there were two tax returns made,—one the Federal and the other the Territorial. In the contract between Mr. Black and E. J. Lord provision was made for apportionment of Territorial and Federal taxes. Now, in this apportionment evidently considerable consideration was given to the amount of taxes to be paid. True, our law is not the Federal law, and income and accounts taxable under our law must be considered only in the light of our law, regardless of what the Federal law may provide, or regardless of what the Federal administration might be. This Board is confined to the Territorial law, but our Territorial law provides for a tax upon capital accounts. Now it is within the province of the Territorial officials to exhaust every effort to ascertain whether or not there has [104] been a capital account in this case, and I submit that this Board would be abusing its discretion if it kept out of the record evidence of the character that we propose to introduce along this particular line.

Mr. PETERS: I might say in regard to that,—might I suggest a way out of the dilemma, to relieve the Board of any embarrassment at this time. I am directing my objection to any imputation, as far as this witness is concerned, that he has treated this situation before the Territorial authorities in one way and has treated it before the Federal authorities in another. May I suggest that as far as Mr. Camp is concerned this objection be sustained for the time being, and then upon the Territory's

(Testimony of H. W. Camp.)

case they can present any facts and figures they want, and then it will come directly before the Board, whether or not they want to rule on this Federal question, and as far as we are concerned, if the Board wants to go into it at that time, we will not object. Can we not have the matter go on at this time without the Board coming to a definite conclusion as to what it will do on this subject, but simply abate the examination of this subject now. Let the matter be resumed if upon the Territory's main case this Board decides it will be glad to go into this entire [105] Federal question. The only thing, we do not want to pass unchallenged any imputation, and that is all it amounts to, any purpose to show that this witness has not acted bona fide in making the returns he did to the Territorial tax officials.

Mr. KAY: I don't recall having made any imputation whatever. It has not been the Board that has exhibited any reluctance to go into this subject, it is counsel. I submit that under the law providing that these hearings are of an informal nature it is the duty of the Board to hear all evidence that may bear upon these questions. The Board has been very lenient to date in admitting all evidence. We would certainly object to any action of the Board in refusing to entertain this evidence.

The CHAIRMAN: Objection overruled.

Mr. PETERS: May it be understood that our objection applies to all this line of examination?

(Testimony of H. W. Camp.)

Mr. WALSH: Certainly. I might say we have a rule here that all formalities are supposed to be omitted as to objections and exceptions.

(Question read by the reporter as follows:

“Will you state whether or not the document I hand you is a true copy of the Federal income tax return made out by you for E. J. Lord for the year 1930?”)

A. That is a true copy of the original return [106] filed by the taxpayer, signed by myself. It is not a copy, however, of the amended return filed for this taxpayer, and that will explain the difference in the figures shown in connection with this transaction and the figures reported on the Territorial return. Unfortunately we don't have a copy of the supplemental Federal return which was filed.

Q. This return was sworn to by you before a Notary Public?

A. It was.

Q. On the back of this return, under Schedule D, will you state what you have entered?

Mr. WRENN: I object to any examination on this return until we get the final return. This shows the error of permitting this kind of evidence.

Mr. ADAMS: I think if there was a supplemental return that should be examined on.

Mr. KAY: I am examining the witness as to an entry made on this return. I think I should be allowed to examine him on it. I think the Board should allow me latitude in making this inquiry.

(Testimony of H. W. Camp.)

Mr. ADAMS: If there was a supplemental return, I think we are filling up the record unnecessarily.

Mr. WALSH: Well, this is a return made by him and I think he should be allowed to examine on it.

Mr. WRENN: This question indicates the real vice [107] of this examination. This cannot lead you anywhere except to confuse the issues.

Mr. KAY: May I state that again, referring to the provisions of the law as to informal hearings. This is not a court of law and I think the Board should allow any evidence that we may have in relation to the issue.

Mr. ADAMS: I think the supplementary return is the one you should examine him on.

Mr. KAY: We may inquire on the supplemental return. We have to start somewhere.

The CHAIRMAN: Objection overruled. Go ahead.

Q. (Question read by the reporter as follows:
“On the back of this return, under Schedule D, will you state what you have entered?”)

A. Schedule D indicates the disposal of 600 shares of E. J. Lord, Limited, stock by the taxpayer, acquired in 1926, disposed of in 1930; amount realized \$599,743.20; cost \$60,000; subsequent charges, \$1,650. That item was legal expense contracted by the taxpayer. Net gain or loss, \$538,093.20. As I say, those figures have been changed in an amended

return which was filed in similar fashion to the change in figures that was made on the Territorial income tax return. The changed items were identically the same in both cases, and the Assessor has full information regarding the change. I would like to state—— [108]

Mr. KAY: Never mind. You have answered the question.

Mr. PETERS: What were you about to say?

Mr. KAY: I submit the witness has answered the question.

The WITNESS: It may develop later. Mr. Kay may ask that question later.

Q. This sale of 600 shares of E. J. Lord, Limited is the same transaction as the subject of inquiry in this case, is that correct?

A. I don't consider it as a sale under Federal law. I consider it as liquidating dividends, which is specifically required to be reported as a gain subject to tax. It is reported as a capital gain on the Federal return, because the Federal law does not require a liquidating dividend to be so reported, but permits the taxpayer, at his option, to consider it as a capital net gain subject to 12½ per cent tax only, and not subject to surtax.

Q. This transaction reported here in this return is the same transaction that is the subject of inquiry in this case?

A. That is correct.

Mr. KAY: We offer this in evidence.

(Testimony of H. W. Camp.)

Mr. WRENN: Objected to, as it is not the final return.

Mr. KAY: We can come to that later return later.

Mr. ADAMS: Why cumber up the record with something [109] that is not relevant?

Mr. KAY: Mr. Adams was not present yesterday, but we did have some forty exhibits introduced by the taxpayer. This is our first exhibit.

Mr. WRENN: That is a very unusual ground for the admissibility of anything in evidence.

Mr. ADAMS: Why not introduce the return on which the taxpayer paid an income tax. He didn't pay it on this. He paid it on his amended returns, did he not?

Q. Was the first installment of the Federal tax paid on the amount shown here in this return?

A. It was.

Mr. ADAMS: That doesn't answer my objection, however.

The CHAIRMAN: Objection overruled.

(Document offered in evidence received and marked: "Tax Assessor's Exhibit "A.")*

(Recess.)

Q. From an accounting standpoint what is surplus considered as? Is it considered as capital or considered as something else?

A. Ordinarily surplus, if the title of the account be "surplus" it is looked upon as indicating accumulated profits of the company which are available for

*Omitted from printed record on stipulation by counsel.

(Testimony of H. W. Camp.)

distribution as dividends. If the caption of the account is "Capital surplus" it [110] indicates that the balance of that account was due generally to contributed surplus, contributed capital at the inception of the company, or inception of the company or business by some transfer to that account of other items than profits of the company.

Q. When earnings are plowed back to a company and go into surplus account they are considered, are they not, as capital?

A. The proportion of those earnings that are plowed back into the company,—the term "plowed back" must mean from an accountant's viewpoint, that the earnings have either been invested in plant or used for operating expenses or in ways other than in distribution of dividends to stockholders.

Q. Is "surplus" confused with the term "working capital"?

A. I don't quite understand your question. Would you mind illustrating in a concrete way what you mean?

Q. Do you know of any instance where surplus has ever been confused, as a matter of terminology, with the working capital?

A. I don't quite understand what you mean by "confused." You mean that surplus is looked upon as working capital?

Q. We will take that construction. Has it ever been looked upon as working capital?

A. Yes, I should think so. [111]

(Testimony of H. W. Camp.)

Q. In 1929 when E. J. Lord, Limited, purchased the 600 shares of stock from E. J. Lord, what account was debited?

A. I can't answer that question. I am not familiar with the opening entries of the books of the corporation at its inception.

Q. Wasn't the treasury account debited?

Mr. PETERS: There is no treasury account. There was some entry as to treasury stock.

A. I think Mr. Buchholtz can answer that question better than I. I am not familiar with the opening entries of the corporation.

Q. Have you any of the balance sheets of the corporation here?

A. No. I think not. I have no balance sheets. The corporation exhibits previously filed would give the complete balance sheets for each year,—filed as exhibits yesterday.

Mr. WRENN: The ones filed with the Treasurer?

A. Yes.

Mr. KAY: I call upon the Taxpayer at this time to produce trial balances for the months January to December, 1930, inclusive; also November and December of 1929. Could those be produced?

Q. Did you have anything to do with the appraisal and net worth of the corporation?

A. I did not.

Redirect Examination [112]

By Heaton L. Wrenn, Esq.

Q. You were put on your cross-examination a hypothetical question by Mr. Kay having to do with

(Testimony of H. W. Camp.)

the sale of Eqa Plantation stock. Mr. Kay spoke of a capital gain in his question. Do you recall any case where they speak of a capital gain?

A. Not in the Territorial law. They speak of a gain. They do not speak of a capital gain.

Q. Will you explain to us what is the difference between the sale of a corporation exchanged between two individuals and the redemption of stock by a corporation, as we have in this case?

A. I consider the two transactions entirely different. A sale of stock by one stockholder to another, as Mr. Kay spoke of, would not affect the accounts of the corporation whatever. There would be no distribution of surplus, no change in the surplus or profit and loss account of the corporation whatsoever; no change in its capital stock account. The outstanding shares would remain the same after the transaction as they were before. The share of the earnings which the stockholder might claim as being entitled to because of his ownership of stock in the company would ride with that stock when the new stockholder acquires that stock. In the case of the disposal of stock owned by a stockholder to a corporation for the purpose of redemption we have an entirely different situation in that case. And I would like to mention here that the [113] redemption of capital stock by a corporation is nothing new in accounting. Dickenson, an eminent English accounting authority, has quite a section in his book on "Accounting Procedure," I believe it is, (I have the book here), setting forth the procedure of

(Testimony of H. W. Camp.)

accounting where capital stock is redeemed. Saliers, an American authority, also covers that subject, and Kester in his volume 2 (I have the title over here but I can't give it at the present time; it is very familiar to all accountants), set forth the way capital stock is redeemed, and all these authorities discuss the effect on a corporation's books in case the stock of one or more of the stockholders may be redeemed. All of them agree that the action of redeeming the stock naturally must result in a change in the capital stock of the company, providing the stock is surrendered and cancelled, and they also show that the interest of the remaining stockholders may be affected. That is to say, their share and interest in the surplus and undivided profits account is directly affected in case that stock is redeemed at a figure other than the par value of the stock, and also providing the payment to the stockholder whose stock is turned in for redemption is not in exact accordance with the proportion of that stockholder's interest in the undivided profits or surplus as indicated by his [114] stockholdings. I believe that sets forth in brief the extreme difference between a sale of stock by one stockholder to another, and the disposition of stock to a corporation for purpose of redemption.

Q. You are familiar with the provisions of the contract of December 13, 1929, are you not?

A. Yes.

Q. And in making up your returns based upon your familiarity with this transaction you con-

(Testimony of H. W. Camp.)

sidered it as a dividend within the meaning of section 1308, revised laws, did you not?

A. That is correct.

Q. You were present when Mr. Kay was stating to the Board the method of taxation of liquidating dividends under the Federal tax laws?

A. Yes.

Q. And you heard the statement he made in regard to how these were taxed?

A. I did.

Q. Will you explain to the Board the condition of the Federal law in this regard, your knowledge of it?

A. Under Federal law a liquidating dividend is considered as resulting in a gain or loss, taxable or deductible, as the case may be, to the stockholders, but the stockholder is not required, under Federal law, to report such gain under Schedule D, [115] which is known as the capital net gain or loss from sale of assets, on the Federal return. As I recall Mr. Kay's statement in that connection, he stated that the Federal law required the taxpayer to report the gain or loss from a liquidating dividend as a capital net gain under this Schedule D. That is not my understanding of the Federal law. I understand that the taxpayer may at his option so report the gain or loss from a liquidating dividend and thereby be subjected to 12½ per cent. tax, but that it is not obligatory for him to do so. He may treat it as subject to sur-tax. I might add may treat it as subject to sur-tax and the normal tax.

(Testimony of H. W. Camp.)

Mr. ADAMS: You mean if he returned it as liquidating dividend it would be subject to normal tax and subject to the sur-tax also?

A. Yes, but he has the option of reporting it as a capital gain if he desires to do so. If his combined sur-tax and normal tax is less than $12\frac{1}{2}$ per cent. he would not do so.

Mr. ADAMS: In other words, you assume the taxpayer in returning his income and in computing the tax that he would return it as a liquidating dividend if it computed at less than $12\frac{1}{2}$ per cent., and, if it computed at more than $12\frac{1}{2}$ per cent. he would return it as a capital net gain?

A. No. I do not mean that. In either case he reports [116] it as a liquidating dividend, but he may report it as under the capital net gain provision. He may report a liquidating dividend as subject to the normal and sur-tax, if the resulting tax would be less than $12\frac{1}{2}$ per cent.; and if it would be more, he may at his option report it under the capital net gain provision as subject to $12\frac{1}{2}$ per cent. tax only. It is so reported as liquidating dividend in either case. Where a stockholder is paid his proportion of the undivided profits and surplus or capital of the company in the nature of a liquidating dividend, I consider it must come under the provisions of the Federal law relative to liquidating dividends and that such a transaction is not exactly the same as the sale of stock from one stockholder to another.

(Testimony of H. W. Camp.)

Q. The condition of the Federal law you have testified to is the Federal law that has existed since 1926?

A. Yes, the 1926 and 1928 Acts are quite the same in that particular respect.

Q. Is not this the case, that the Federal income tax law does not in any way seek to change the character of a liquidating dividend, but merely permits you to treat it as capital gain for taxation purposes?

A. Yes. [117]

Q. What was the situation under the Federal law in regard to liquidating dividends prior to the change made in 1926?

A. There have been quite a number of changes in prior acts. At one time they were taxed as ordinary dividends.

Q. Even when the law said "Gains from all other sources" they were taxed as ordinary dividends?

A. There was a specific provision that liquidating dividends should be taxed as ordinary dividends and subjected to the sur-tax.

Q. In connection with your explanation of the Federal income tax laws, I call your attention to Article 624 of regulation 74, Federal income tax regulations. I would like to have you read that.

A. I am reading from regulation 74 issued by the Treasury department relative to the Revenue Act of 1928. This is the Treasury department regu-

(Testimony of H. W. Camp.)

lations governing the Federal income tax law. "Article 625". Headed "Distribution in liquidation": "Amounts distributed in complete liquidation of a corporation are to be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation are to be treated as in part or full payment in exchange for the stock so cancelled or redeemed." The phrase "amounts distributed in partial liquidation" means a distribution of a corporation in complete cancellation or [118] redemption of a part of its stock, or one of a series of distribution in complete cancellation or redemption of all or a portion of its stock. A complete cancellation or redemption of a part of the corporate stock may be accomplished, for example, by the complete retirement of all the shares or a particular preference or series or by taking up all of the shares of a particular preference or series and issuing new shares to replace a portion thereof, or by the complete retirement of any part of the stock whether or not pro rata among the stockholders." That is the section of that article which I would like to place before you for consideration. I will read one more paragraph: "The gain or loss to a shareholder from distribution in liquidation is to be determined as provided in Section 111, Article 561, by comparing the amount of distribution with the cost or other basis of the stock, provided in Section 113, Articles 591 to 604, but the gain or loss will be recognized only to the extent

(Testimony of H. W. Camp.)

provided in Section 112, and Articles 571 to 580. Any gain to the shareholder may at his option be taxed as a capital net gain in the manner and subject to the conditions prescribed in Section 101 and Articles 501 to 503''. I will not read further, because this article goes on to cite certain examples, and has reference to distributions [119] in case of reorganization which I consider does not bear on the case. I would like to point out that this resolution speaks of the redemption of capital stock, either partially or in full, in complete retirement of one shareholders stock or more than one.

Q. Does the regulation which you have just read in the Federal income tax act apply to voluntary as well as involuntary redemptions of stock?

A. Yes, I should say so.

Recross Examination by Harold T. Kay, Esq.

Q. In your opinion this payment made by E. J. Lord, Limited, To E. J. Lord, was not a capital net gain but was a liquidating dividend?

A. Yes. In viewing it from Section 1391 I believe it is. In the Territorial law it is a liquidating dividend, the same under Federal law also.

Q. Have we any such term in our Territorial law as "liquidating dividend"?

A. No, not that I know of.

Q. We do tax capital net gains under our law?

A. You tax gains and profits.

Q. In 1390 there is a provision that all gains from the sale of moveable property are taxable?

(Testimony of H. W. Camp.)

A. The law will speak for itself on that. I think that is so. I don't know the exact wording of the law, but in general gains from sale of assets from [120] one individual to another, or one corporation to another, are subject to tax, providing there is a profit on them, and where they do not involve the distribution of undivided profits to the stockholder.

Q. Under the Federal law is it not a fact that the terms "Liquidating dividends" and "Sale of capital assets" are used synonymously to represent the same thing?

A. I would not say that.

Mr. PETERS: I object to that. It seems to me we are getting into the realm of speculation here, asking the witness to determine those things which the Board will be ultimately called upon to determine. As far as we are concerned, if the Board feels that these references to the Federal law are material, we have no objection, but to ask the witness what construction he puts on the terms in the different laws seems to me is asking the witness to put construction on things which it is the province of the Board to determine. As a matter of fact, as to whether or not a liquidating dividend is the same dividend under the Territorial law is another question for the Board to decide, and, obviously, that Board can conceive right now of liquidating dividends in some instance containing capital, but when the liquidation comes in partial liquidation of stock it may also contain capital, [121] and under the law

(Testimony of H. W. Camp.)

it does not make any difference in the Federal law, but under the Territorial law you must deduct the portion that is capital and it only applies to what it apparently profits, in dividends.

Mr. ADAMS: The witness is qualified as an expert accountant.

Mr. PETERS: If it is just from an accountancy standpoint I have no objection.

Mr. ADAMS: And one who is qualified to make Federal returns.

Mr. PETERS: If it is from that standpoint, as to whether or not it is from an accountancy standpoint, the objection is not well taken.

Q. (Question read by the reporter as follows: "Under the Federal law is it not a fact that the terms "Liquidating dividends" and "Sale of capital assets" are used synonymously to represent the same thing?)"

A. My answer was incomplete owing to the objection taken at that time. I would not say so, for this reason: My understanding of the Federal law is that liquidating dividends and any resulting gain from such liquidating dividends to the taxpayer, must, under Federal law, be returned,—the gain must be reported the same as if the stockholder had sold his stock. That is my understanding of the [122] Federal requirements. The Federal law does not say, however, that a liquidating dividend is a sale of stock. It merely requires that the stockholder reports his gain or loss from that transaction

(Testimony of H. W. Camp.)

in the same way as if he disposed of his stock in some other way, than obtaining his distribution from the surplus of the company. Does that answer your question, Mr. Kay?

Q. Not quite. Doesn't a liquidating dividend represent a distribution of assets?

A. It must. If the company pays out cash it is bound to.

Q. And the gain on that distribution is measured by the price paid and the value distributed, isn't that correct?

A. Under Federal law there are a good many provisions affecting the determination of that question. First of all it depends on when the stock was acquired, how it was acquired, whether it was acquired prior to August 1, 1913, or subsequent thereto, whether it was acquired by gift prior to December 31, 1920, or subsequent thereto. It further depends on whether or not the corporation has issued any distributions which are not subject to tax under Federal law, any partial liquidating dividends which may have been declared between the time the stockholder acquired his stock and the time he received his final distribution must [123] have the effect of reducing the cost.

Q. In any event, the gain is measured by the cost to the stockholder of his stock and the value of the distribution to him?

A. I would qualify that by saying that the cost, as governed by the provisions of the Federal tax

(Testimony of H. W. Camp.)

law, the cost as determined under Federal law, not the exact cost to the taxpayer in dollars and cents.

Q. We will say the basis of the cost, then?

A. Will you give that question again, please.

Q. (Question read by the reporter)

A. Yes.

Q. And that gain is not considered as a taxable dividend under Federal law, is it?

A. Yes, it is considered as a liquidating dividend subject to tax.

Q. Isn't it—a liquidating dividend—used in a different sense from that of the regular taxable dividend declared by a corporation in its usual course of business from net profits?

Mr. PETERS: That is what we have been contending for right along.

Mr. WALSH: Let him answer the question.

A. I would like to have the question read again.

Q. (Question read by the reporter)

A. A liquidating dividend is a regular taxable dividend. I cannot see we can divide,—there is nothing [124] I understand in the Federal law that speaks of a regular taxable dividend on one hand and a regular liquidating dividend on the other. They are both taxable dividends.

Q. Where is the term liquidating dividend usually used for the purpose of making out tax returns?

A. It applies to situations such as I read from the regulations, article 625, a moment ago. Where

(Testimony of H. W. Camp.)

there is a partial distribution of the company's assets in redemption of a part or all of stockholders' stock that liquidating dividend may be paid out of surplus; it may be only a partial distribution. If it is paid out of certain reserves the Federal law permits a distribution out of certain reserves in such a way that they shall not be subject to Federal income tax. You may have liquidating dividends in that sort of situation.

Q. Essentially, however, a liquidating dividend is a distribution of assets?

A. It is a distribution of assets purchased out of accumulated earnings of the corporation,—assets which have resulted from plowing in of profits of the corporation.

Q. Can liquidated dividend be made from capital?

A. Yes, then you have a situation of reducing the capital stock. When you say "capital" I assume you mean out of capital stock resulting in reduction of capital stock and returning to the taxpayer his [125] par value of the investment.

Q. So any distribution may be considered a liquidating dividend?

A. No, not in Federal law or Territorial law. A cash distribution reduces the surplus, but it is not a liquidating dividend.

Q. Are you familiar with Prentiss-Hall "Federal Cumulative Tax Service" volume 2 of the Edition of 1929?

(Testimony of H. W. Camp.)

A. I am not, but I am familiar with the Corporation Clearing House Service and the two services are very similar.

Q. Referring to volume 2 of this service, page 9051, section 115, article 629, entitled "Distributions", being the Federal regulations, and examples thereunder, the following is said: "On the other hand, a cancellation or redemption by a corporation of all the stock of a particular shareholder so the shareholder ceases to be interested in the affairs of the corporation does not effect the distribution of a taxable dividend". Will you state whether or not that statement conforms to your idea in respect to that matter?

A. I will state that that section of Article 629 specifically mentions that where the distribution and cancellation or redemption in whole or in part is essentially equivalent to the distribution of a taxable dividend, then the amount so distributed [126] in redemption or cancellation of the stock shall be treated as a taxable dividend. I quite agree with that, but I should like to point out that is only in those situations where the distribution is essentially equivalent to the distribution of the taxable dividend, and if Mr. Kay will look in Prentiss-Hall in the second paragraph he will find this statement: "On the other hand, a cancellation or redemption by a corporation of all the stock of a particular shareholder, so the shareholder ceased to be in-

(Testimony of H. W. Camp.)

terested in the affairs of the corporation, does not affect the distribution of a taxable dividend.”

Mr. WALSH: That is the question he asks you.

A. In that particular situation the Federal law goes on to subject the liquidating dividend to the tax as a liquidating dividend.

Q. And that tax cannot be less than the tax on capital net gain, can it?

A. Yes, certainly.

Q. Is it not provided in the Federal law it cannot be less?

A. No, the capital net gain is optional to the taxpayer. It is an optional provision, as I understand it. The taxpayer does not have to report the gain from the disposal of any asset there in any way whatever. He is not required to report it as a [127] capital net gain subject to the 12½ per cent. tax.

Mr. ADAMS: You mean if you treat it as dividend, it is subject to the normal tax and surtax, if the tax is less than 12½ per cent. then you don't have to report it as a capital net gain?

A. That is my understanding.

Mr. ADAMS: So he need not report it as a capital gain?

A. That is my understanding.

Q. In your Federal income tax return if the Federal law would have required a less tax why

(Testimony of H. W. Camp.)

would not this gain be reported as a liquidating dividend?

A. This transaction was reported as liquidating dividend. The taxpayer through his agent choose to elect that gain be taxed under the capital net gain tax rate which is $12\frac{1}{2}$ per cent. That is the very situation covered by this article. It permits the taxpayer, if he would be taxed a greater amount than under the normal and sur-tax rates it is not classed as an ordinary taxable dividend, but it may be considered as a transaction that he may at his option select to be taxed $12\frac{1}{2}$ per cent. Necessarily the taxpayer would not select that option to be taxed under the capital net gain provision nor would he have paid it under section "D" if he had reported it subject to the normal and sur-tax rates. [128]

Mr. PETERS: Let me understand it. May I ask the witness a question to clear it up?

Mr. KAY: There are two or three questions I would like to ask in connection with the witness.

Mr. PETERS: I don't understand the answer of the witness at all. Perhaps your questions will clarify that question.

Q. Unless this transaction were within the class of capital net gain transactions it could not have been reported as a capital net gain transaction, could it?

A. The regulations provide that this particular kind of a transaction may be reported as a capital net gain.

(Testimony of H. W. Camp.)

Q. In other words, they consider that type of transaction as within the class of capital net gain transactions, that is correct, is it not?

A. That is my understanding of the law. They don't limit it to a capital net gain. A capital net gain transaction is one where a taxpayer disposes of capital assets which he has held for more than two years prior to date of sale. It is purely an optional provision in the law and the taxpayer does not have to report his transaction as a capital net gain. He simply reports the gain as subject to tax. He must report it subject to tax, but not necessarily as a capital net gain. The law requires him to report the gain and the liquidating dividend, measured [129] by the difference between the cost basis and the amount received in liquidation. That is classified as a taxable gain. As far as the taxpayer is concerned, he may report it in any way he likes on his tax return, but the regulations specifically provide, article 629, specifically provides that where a corporation distributes amounts to a taxpayer in full or partial liquidation of his stock,—I don't mean partial liquidation, I mean in complete retirement of his stock—that consideration shall not be construed as a taxable dividend, therefore that provision enables,—and if it were not for that provision the taxpayer could not possibly take advantage of the capital net gain of 12½ per cent.,—but that provision specifically enables him to report that net gain under the capital net gain tax rate.

(Testimony of H. W. Camp.)

Q. Under the Federal law a liquidating dividend may entitle the taxpayer to claim a loss, may it not?

A. Yes.

Q. Do you know of any provision in our law that contemplates or considers any dividend paid by a corporation of the nature or having the nature of a loss to the recipient?

A. No, I don't know of any provision allowing a loss to the recipient. In a case of that kind our law is not very specific. In the matter of dividends it does not specify the difference between ordinary [130] dividends and liquidating dividends, or dividends declared from depreciation, depletion or depletion reserve.

Q. Are you familiar with section 1361, Revised Laws of Hawaii, providing for the duties of managers of corporations. Will you examine that and state whether or not you are familiar with that provision?

Mr. WRENN: I object to getting off on this other angle of this case. That is a section on corporations that has to do with the liability of directors to declare dividends, which may impair the assets of the corporations. This has nothing to do with any of the issues before the Board. That is something a tax man is not interested in.

The CHAIRMAN: Objection sustained.

(Adjourned to 9 o'clock a.m., Monday, December 7, 1931.) [131]

(Testimony of H. W. Camp.)

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Monday, December 7, 1931, at 9:40 o'clock a.m., all Members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

Mr. KAY: The Government did not make preparations to go ahead this morning, as I understood this case would not go on this morning. We are willing to accommodate counsel and the Board this morning and go ahead as far as we can, if the Board so desires.

The CHAIRMAN: Go ahead with it.

Mr. WRENN: We should like to go on.

GEORGE BUCHHOLITZ,

a witness for the Taxpayer, resumed the stand and testified as follows:

Cross Examination by Harold T. Kay, Esq.

Q. How long have you been Secretary of E. J. Lord, Limited?

A. Since the time of incorporation.

Q. What is your official title, Mr. Buchholtz?

[132]

A. Treasurer at that time. Now I am Treasurer and Secretary.

(Testimony of George Buchholtz.)

Q. E. J. Lord, Limited, was incorporated back in 1926, was it?

A. Yes.

Q. Who were the stockholders at that time?

A. Time of the incorporation?

Q. Yes.

A. Mr. Lord, Mr. Black, myself, Mr. Ikejiri, and I think Mr. Erbes.

Q. And the stock held by these respective stockholders was how much?

A. Mr. Lord had originally 797 shares, to the best of my recollection. Mr. Black had 200 shares, and these other three had one share each.

Q. How were those shares paid for?

A. Mr. Lord had a certain amount of plant that was turned into the capital, which was valued at—

Mr. PETERS: May I suggest if you consider this material that the witness have the affidavit of the corporation so the exact figures may come to the Board. The entire matter is set forth in the affidavit of the corporation, and according to the evidence of Mr. Buchholtz the figures were compiled by him, so as long as the Board is considering this evidence, it might just as well have it properly before us as otherwise.

Mr. WRENN: I would like to have it stated at this time [133] that this question of the original contribution is not before the Board. Mr. Glass has admitted that the sixty thousand dollars received was equal to his original capital contribution. It is just another phase of the matter that we are not

(Testimony of George Buchholtz.)

concerned with whatever. That is one thing the pleadings admit. I submit we can get nothing that will assist the Board by going into this original contribution, when the figures the Board has and Mr. Glass has admitted that the figures were sixty thousand dollars in making up his original assessment.

Mr. KAY: I submit the question is relevant.

Mr. WRENN: I would like to have a ruling on that by the Board.

The CHAIRMAN: Do you object to the question?

Mr. WRENN: Yes, it is incompetent, irrelevant and immaterial. The facts are admitted.

Mr. ADAMS: This plant, in the articles of incorporation, is valued at sixty thousand dollars?

A. I can't remember those. It is quite a complicated affair. (Referring to affidavit.)

Mr. WRENN: Your question refers now to the time this deal went through?

Mr. ADAMS: Yes.

Mr. WRENN: The question is whether or not his capital contribution was valued at sixty thousand dollars at the time this deal went on? [134]

Mr. WALSH: No, that's not the question.

The WITNESS: What deal?

Mr. PETERS: The option of December, 1929.

A. Mr. Lord had sixty thousand dollars worth of stock at that time.

(Question and answer read.)

(Testimony of George Buchholtz.)

The WITNESS: Had eighty thousand dollars.

The CHAIRMAN: Objection sustained.

Mr. KAY: May it please the Board, we would like to have an understanding at this time as to what—

The CHAIRMAN: As I understand, Mr. Glass had admitted all of these figures.

Mr. KAY: There have been no admissions by Mr. Glass.

Mr. PETERS: He has admitted it in his assessment.

Mr. KAY: This is a matter of cross-examination and we should know what he paid for that stock at that time.

Mr. WRENN: All you have to do is to ask Mr. Glass if he hasn't admitted it in his assessment.

Mr. WALSH: That is immaterial. This document has been admitted in evidence and we have the right to discuss it.

Mr. PETERS: That may be true in a certain sense. I take it that affidavit is not subject to impeachment.

Mr. WALSH: There is no question of impeachment.

Mr. PETERS: If there is no question of impeachment here should this matter be gone into? This is [135] immaterial, because it is all set forth here. The affidavit of incorporation of E. J. Lord, Limited, states who the officers are, the number of shares and the cash that has been paid for three of the shares. Listen to this language:

(Testimony of George Buchholtz.)

“That \$300. has been paid in cash for three of the said shares and it is intended that before the company engages in business that all the personal property hereinafter more particularly described forming and used as a general contracting and engineering business in the Territory of Hawaii, and heretofore carried on under the name ‘E. J. Lord’ will be assigned to the company by said Edmund J. Lord in exchange for 800 shares to be issued to him as fully paid up and non-assessable in exchange for said property, and that a promissory note for the sum of \$20,000. dated July 31, 1926, made by the said Edmund J. Lord payable on demand to said Everett E. Black, without interest, and constituting a debt payable by said business, will be paid by the said Company by issuing to said Everett E. Black 197 shares of said Company, as fully paid up and non-assessable, and by the payment by the Company of \$300 in cash to said Everett E. Black in exchange for said promissory note, which will then be delivered to the Company and cancelled as paid. The object of the incorporation of E. J. Lord, Ltd., is to take over and conduct as a going concern the general contracting and engineering business now carried on in the Territory of Hawaii by the said Edmund J. Lord under the name of ‘E. J. Lord,’ a full description of the property comprising which, and intended to represent 80% of the capital stock of the proposed corporation and

(Testimony of George Buchholtz.)

a detailed valuation of each item of said property is as follows: Assets: Accounts Receivable" so much; Contracts Receivable; Contracts a/c Reserves; Personal Accounts Receivable; Plans and Specifications; Cash on Hand; Prepaid Insurance; Supplies and Materials; Plant and Equipment; Less Depreciation Reserve; Office Building, Kakaako; Furniture and Fixtures; Auto and Tool Shed; Kakaako; Good Will;" making a total of \$254,997.03. "Less liabilities, etc., \$105,997.03 and Notes Payable, \$69,000.," making \$174,997.03, showing net total of \$80,000. * * * "Also the object of incorporation of said E. J. Lord, Ltd., is to take over and pay the said promissory note for \$20,000. dated July 31, 1926, made by the said Edmund J. Lord payable on demand to the said Everett E. Black or order, said promissory note to be paid by the Company by the issue of stock and \$300. in cash, as stated above." [136]

And then follows the conveyance from Edmund J. Lord to E. J. Lord, Limited. Now we have gone right through, down through the history of the corporation, until we come, as Mr. Wrenn has properly called to the attention of the Board, to the figures as they are contained in the return, and as far as I understand it there has been no objection made by Mr. Glass to the figures as returned by the taxpayer, showing that the capital as represented in the amount received by E. J. Lord in redemption of his stock as sixty thousand dollars.

(Testimony of George Buchholtz.)

Mr. ADAMS: After all these deductions there were assets of eighty thousand dollars, less a promissory note of twenty thousand, which makes sixty thousand dollars, and in this computation by the tax assessor are the figures sixty thousand dollars.

Mr. KAY: I think counsel is anticipating the object of this particular inquiry. It is not to attack the value of the property transferred, but the nature and the character of that property, and as far as the issues are concerned we have no intention to challenge the value of the property. Mr. Glass, it is true, has not challenged the value, to-wit, sixty thousand dollars, but when all this mass of stuff is thrown into evidence, I think 44 exhibits, containing a great deal of data and so forth, data that has not been explained in direct examination, certainly we have the right on cross to inquire [137] into that particular data, the character and nature of it, and if the Board has permitted holus bolus the admission of all this data, I don't think the Board, in fairness to the Government, should refuse an examination into the character and nature of the data.

Mr. PETERS: I don't think there is any question as to the character of this property that was turned in.

Mr. WALSH: Why not let the witness answer that question. You have answered it twice, but why not let the witness answer it.

Mr. WRENN: My point is that at the last hearing we objected to going into the question of Federal

(Testimony of George Buchholtz.)

income tax and we spent two days on it. Now we may spend two days on this.

Mr. KAY: I haven't heard a statement of the issues made by opposing counsel to this Board.

Mr. WALSH: We will assume the issues by reading the appeal, but counsel haven't announced the issues.

Q. Included among this property turned over by Mr. Lord there were various contracts, were there not?

Mr. WRENN: Same objection.

Mr. PETERS: You are speaking now of 1926?

Mr. KAY: Yes.

Mr. ADAMS: I think we are wasting a lot of time. It is all set forth in the affidavit and it is boiled down in the tax assessor's admission of eighty [138] thousand dollars. It all boils down to eighty thousand dollars, less the promissory note for twenty thousand dollars, which gives sixty thousand as the value of the stock.

Mr. KAY: I do not desire to unnecessarily prolong the subject of inquiry. I think I could dispose of it in about two minutes. I might state that in direct examination counsel has gone to considerable extent in endeavoring to build up the fact that only earnings have gone into this surplus account from which they contend payment was made to Mr. Lord. They have gone into the history of the corporation, the financial set-up and the character of the various accounts. I think we are perfectly proper in making inquiry into the origin of the property of the cor-

(Testimony of George Buchholtz.)

poration. If the Board does not care to have us proceed along that line, we will defer to the wishes of the Board. If the Board does not feel it is relevant, we do not desire to unnecessarily take up the time.

Mr. WRENN: If Mr. Kay will make an offer of proof that any of the \$468,000. distributed to Mr. Lord is capital, I will withdraw any objection, but I do object to his going on a fishing expedition when it will serve no good purpose. Mr. Glass has taken the amount of capital as sixty thousand dollars. The only question is whether the difference between [139] the sixty thousand dollars and the \$468,000. was an amount on which an income tax has been paid. That is the only difference between his assessment and the return which was made by the taxpayer.

The CHAIRMAN: Objection sustained.

Mr. KAY: May we have our objection to the ruling of the Board.

Q. Turning to Taxpayer's Exhibit 34 for the year 1926 is any of that income there noted under the column of 1926 derived from the contracts assigned by Mr. E. J. Lord to E. J. Lord, Limited?

A. I will have to look that up. I don't know whether any contracts went over or not. I can't remember that off-hand.

Mr. PETERS: Do I understand from your question that the contracts are considered by you as capital gain and hence not income? Otherwise, it seems to me, if the Board please, that this question

(Testimony of George Buchholtz.)

is objectionable on the same ground as raised by Mr. Wrenn. I think the position of the taxpayer should affirmatively appear on the record that if there is any item, offer or proof of which Mr. Kay desires to make, contained in the surplus account that is not surplus profits, but, on the other hand, is capital, we are willing to meet that issue, but, in the absence of any offer to meet that issue it seems to me it comes within the objection we raised.

Mr. KAY: Is the Board going to proceed along the [140] lines already adopted by it, to-wit, informal proceedings, allowing parties to make objections and take exceptions and proceed, or allow these objections to be made and refuse counsel to inquire into the subject matter already presented by opposite counsel.

Mr. ADAMS: I don't think that question is objectionable.

Q. Will you make an examination of your books?

A. I can answer that question now. There were certain contracts taken over from E. J. Lord to E. J. Lord, Limited. They were closed up entirely up to that date and any profits or losses on those contracts went into profit and loss.

Q. In what year would those profits appear, if any?

A. 1926.

Q. Were there any profits made on those contracts in 1927?

A. I think they were all completed in 1926. I am not positive of that, but I think they were all completed.

(Testimony of George Buchholtz.)

Q. Will you make an examination before our next hearing and be prepared to state whether or not they were all closed out in 1926? Now, in 1926, 1927 and 1928 dividends were declared by your corporation, were they?

A. Yes. [141]

Q. How were those dividends declared?

A. How they were declared?

Q. Yes, what was the procedure?

A. The minutes show they were authorized to be paid in the meetings.

Q. What were the proceedings in these meetings?

A. Declaration of dividends from the surplus.

Q. Was that declaration duly noted in the minutes?

A. Yes, sir.

Q. Have you got a form of the usual declaration of dividend as contained in your minutes?

A. The regular form? No, the meetings were called at different times to declare the dividends. There was no regular form.

Q. It would appear in the minutes?

A. Yes.

Q. And that dividend would be payable to the stockholders according to the amount of stock held by them?

A. Yes.

Q. At the time of this agreement with Mr. Lord in 1929 was there any declaration of dividends?

A. I haven't quite got your question. In what time in 1929?

(Testimony of George Buchholtz.)

Q. Any time in 1929?

A. I think there were dividends declared in 1929, yes. The statements here will show that. May I look [142] at that dividend and surplus account for a minute. (Witness examines paper) 1929,—yes, dividends were declared.

Mr. WALSH: How much?

A. On March 31st \$30,000.; April, \$50,000.; May, \$70,000.; total \$150,000.

Mr. WALSH: March, April and May.

Q. Does the payment to Mr. Lord appear in the minutes as a dividend declared by the corporation in 1930?

A. It does not appear.

Mr. PETERS: We will admit it appears as a redemption of stock.

Q. Let the witness answer that.

A. I will have to examine again. (Witness examines papers) Mr. Lord did not receive any dividend in 1930. \$25,000, was paid to Mr. Black. Are you referring to liquidating dividends?

Q. No, I am referring to dividends.

A. There were \$25,000. paid to Mr. Black.

Q. So that in the year 1930 the only dividend declared was a dividend of \$25,000?

A. Only regular dividend.

Mr. WALSH: Was there any special dividend?

A. There was a liquidating dividend paid.

Mr. WALSH: Declared?

A. Declared. [143]

(Testimony of George Buchholtz.)

Q. In the year 1930?

A. No, it was paid in 1931, I guess.

Q. There was no dividend declared in 1930?

A. That \$25,000. was declared.

Q. That was the only dividend of any character whatsoever declared in the year 1930?

A. Yes.

Mr. KAY: May it please the Court, counsel has introduced a great mass of material here, that I haven't had an opportunity of examining fully, and I would like to have the privilege of deferring further cross-examination of this witness until our next hearing, assuming I feel it necessary, giving me an opportunity of completing my examination of all these exhibits. The Board will recall that a lot of these exhibits were introduced without objection on our part, subject, however, to my examination. We haven't had an opportunity to make a full examination.

The CHAIRMAN: There is no objection to that.

Mr. PETERS: We understand that our redirect examination of Mr. Buchholtz is left entirely open. This matter of dividends that has been gone into this morning, we should like to go into that.

Mr. WRENN: We will reserve that on our full redirect-examination when he is through with cross.

(Witness withdrawn.)

Mr. WRENN: I offer in evidence minutes special meeting [144] of the Board of Directors of

(Testimony of George Buchholtz.)

E. J. Black, Limited, held at the office on December 5, 1930, at 11 o'clock a. m.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 37D.")

TAXPAYER'S EXHIBIT 37-D

MINUTES of a Special Meeting of the Board of Directors of E. E. Black, Ltd., held at the office of the company on December 5th, 1930 at 11 A. M.

PRESENT:

Mr. E. E. Black, President
" Geo. Buchholtz, Treasurer
" T. Ikejiri, Secretary

CHAIRMAN:

There being a quorum present, Mr. Black took the chair and called the meeting to order.

MINUTES OF AUGUST 13th, 1930:

The minutes of a Special meeting of August 13th, 1930 were read, approved and ordered placed on file.

ADDITIONAL PAYMENT FOR PLANT TO MR. E. J. LORD:

Mr. Black stated that Mr. Lord for some time past had been requesting an additional sum of over \$12,000.00 for Plant in the first part of his settlement, on account of there being items of Plant in existence, which were not shown in the Plant Account, and whereas Mr. Lord was willing to compromise for the sum

(Testimony of George Buchholtz.)

of \$3,500.00 suggested acceptance. Mr. Buchholtz moved that the offer to compromise for \$3,500.00 be accepted and paid at the time of the final settlement, Mr. Black seconded the motion, carried unanimously.

ADJOURNMENT:

There being no further business the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary. [313]

Mr. KAY: May this offer carry our reservation also of examination.

The CHAIRMAN: Yes.

E. E. BLACK

was duly called and sworn as a witness for the Taxpayer, and testified as follows:

Direct Examination by Heaton L. Wrenn, Esq.

Q. You are E. E. Black?

A. I am.

Q. You own all the capital stock of E. E. Black, Ltd.?

A. I do.

Q. Formerly you owned 40 per cent. of the stock of E. J. Lord, Limited?

A. Yes.

(Testimony of E. E. Black.)

Q. You are not a tax expert, are you?

A. No.

Q. Nor are you an accountant?

A. No, and I am not an attorney either.

Q. You are just a common garden variety of engineer?

Q. In the early part of December, 1929, E. J. Lord, [145] Limited, had certain negotiations with Mr. E. J. Lord relative to his retiring from business, did they not?

A. Yes.

Q. Was it the intention of E. J. Lord, Limited, at that time, when the deal was finally consummated by the preparation of an option on December 13, 1929, to redeem the capital stock held by Mr. E. J. Lord?

A. It was, because it was representing my ambition of a life-time to own my own company.

Q. And the idea was then to pay Mr. Lord in the matter of the redemption of his stock his capital contribution plus his share of the earnings in the company?

A. That is quite right, and the contracts pending.

Q. And after his stock had been redeemed, to retire it and reduce the capitalization to equal the 400 shares you owned in the company?

A. That is quite right.

Q. And further to change the name of the company to E. E. Black, Limited?

A. Yes.

(Testimony of E. E. Black.)

Q. And after the capital stock had been fully redeemed by paying Mr. Lord his sixty thousand dollars and his share of the profits as well as his share of the contracts completed in the year 1930, the capital stock of E. E. Black, Limited, was then [146] reduced, was it not?

A. Yes.

Q. At the time that Mr. Lord owned his stock in E. J. Lord, Limited, you and he were the only real stockholders in the company?

A. Yes.

Q. And the other three persons who held a share of stock apiece held it merely nominally and were dummies?

A. Yes.

Cross Examination by Harold T. Kay, Esq.

Q. Prior to the incorporation of E. J. Lord, Limited, you and Mr. Lord were partners, were you not?

A. No, I worked for Mr. Lord on a salary and a percentage of profits.

Q. And when E. J. Lord, Limited, was incorporated Mr. Lord transferred to E. J. Lord, Limited, the entire business carried on by him?

A. Yes.

Q. And he received in payment of that approximately 800 shares?

A. I can't tell you the exact details of that. It finally worked down to his owning 600 shares and my 400, and part of my 400 was paid off by my percentage of the earnings.

(Testimony of E. E. Black.)

Q. In other words, he owed you money and you turned over to him the particular obligation that he owed [147] you in consideration of his turning over to you a certain amount of stock of E. J. Lord, Limited?

A. Yes.

Q. In other words, you cancelled the obligation he owed you?

A. That is the company.

Q. But it was an individual transaction between the two of you, where he turned over part of his own stock to you, wasn't it?

A. At the very beginning. I think that was only at the beginning.

Q. So the final result was that you owned 400 shares and he owned 600?

A. That's right.

Q. And that relationship in respect to the amount of stock owned by each of you continued until 1929?

A. Yes.

Q. And in 1929 you desired to own your own business and proposed to Mr. Lord to buy him out?

A. That's right. I would not say particularly "buy" because the whole assets of the company were divided 60-40 as best we could. I agreed with Mr. Lord to take the plant, as he was going out of the contracting business, and that value was established, and with the bonds and cash we had that pro-rated 60-40.

(Testimony of E. E. Black.)

Q. In other words, Mr. Lord was contemplating [148] retiring from the contracting business at that time?

A. Yes. It was not a forced sale. Very agreeable.

Q. Might I suggest to you that there was a proposition made that either you buy Mr. Lord out or he buy you out, the two of you couldn't continue on together in the business?

A. No.

Q. Then the proposition was he wanted to get out of the business and wanted to sell to you his interest?

A. Yes. We had had an agreement previously before this was drawn if anything happened to Mr. Lord or to me we would have the first refusal of the stock, and Mr. Lord was not in very good health at that time, and he had at that time more assets than he ever had before in his life, and it was the logical time for him to retire.

Q. So it was proposed that E. J. Lord, Limited, buy Mr. Lord's stock, paying him with assets of E. J. Lord, Limited?

A. I don't know whether you are trying to get technical with me or not?

Q. No, I am not.

A. It was just a division of the assets of the company, plant, stock, bonds and cash, sixty-forty. That is what it amounted to.

Q. In other words, the company would pay to Mr. Lord [149] sixty per cent. of the value of everything the company had?

(Testimony of E. E. Black.)

A. That's right, for the surrender of his stock to E. J. Lord, Limited, which after the first of the year was E. E. Black, Limited, with the understanding that I would take the plant and the stuff, all our legal assets.

Mr. PETERS: When you say "I" you mean E. E. Black, Limited?

A. Yes, E. E. Black, Limited.

(Recess)

Q. I understand from your direct examination, Mr. Black, that this transaction between E. J. Lord, Limited and E. J. Lord, was a transaction whereby E. J. Lord would sell to E. J. Lord, Limited, the 600 shares of stock, and that it was to be paid for by E. J. Lord, Limited, in the assets of the company, and apportioned on a basis of 60 per cent. of net worth and that in your agreement executed in 1929 with Mr. Lord the net worth was to be determined pursuant to amicable arrangements between the parties and that the Territorial and Federal taxes were to be born in the same ratio by E. J. Lord, Limited, and E. J. Lord,—that is to say, 60-40, that is correct?

A. That's correct.

Q. I think you have already made the statement that you are not a tax expert or an attorney or [150] anything but just an engineer, and consequently you left these tax matters and so forth to your legal and tax expert advisors, didn't you?

A. That's quite right. All I do is to take the responsibilities.

(Testimony of E. E. Black.)

Q. And pay them?

A. Yes.

Redirect Examination by Heaton L. Wrenn, Esq.

Q. When you answered several of Mr. Kay's questions you spoke of yourself, what you were to get out of it. You meant what E. J. Lord, Limited, would, didn't you? You personally didn't play any part in this deal?

A. No, only I represented E. J. Lord, Limited.

Q. The deal was between the corporation and Mr. E. J. Lord?

A. That's right.

Q. In regards to the original purchase of your stock before the incorporation of E. J. Lord, Limited in 1926, you actually paid twenty thousand dollars in cold cash out of your pocket, your own pocket?

A. It was cash I had earned.

Q. Whatever you got you paid for yourself?

A. Yes.

Recross Examination by Harold T. Kay, Esq.

Q. E. J. Lord, Limited, at the time of the execution [151] of this agreement with E. J. Lord in 1929 was a going concern, carrying on a general contracting business here in the Territory?

A. Yes.

Q. And there was considerable business on the books at that time too, was there not?

(Testimony of E. E. Black.)

A. Yes, Mr. Lord had a 60 per cent interest in the jobs that extended over the end of 1929. That was part of the agreement.

Q. You had during the years that E. J. Lord Limited had been incorporated and doing business, you had taken a much more active part in the business than Mr. Lord, did you not?

A. I guess you could say that. I was vice president of it, but Mr. Lord left the execution of the work pretty much up to me. He acted pretty much in an advisory capacity. Before that he was in poor health and had family troubles as well.

Q. As a matter of fact, without being too modest, you were responsible largely for the building up of the business of E. J. Lord, Limited?

A. Oh, I would not say that.

Mr. ADAMS: This E. J. Lord, Limited, took over a certain amount of plant and equipment, didn't you?

A. Yes, it was a going contracting concern of E. J. Lord?

Mr. ADAMS: I mean when you negotiated for the retirement of E. J. Lord as an individual you listed [152] a certain amount of plant and equipment as being of a certain value?

A. Yes, we carry that all the time; depreciate it every month.

Mr. ADAMS: Approximately what was that value?

A. Some sixty-five thousand dollars.

Mr. ADAMS: That accounts for the payment, or whatever it may be, retirement of E. J. Lord's

(Testimony of E. E. Black.)

original stock? The value of his original stock was approximately \$60,000. of plant?

A. There had been considerably large plant bought and the original plant was depreciated on book value and some was obsolete and worn-out. This plant account we had then I don't think had any connection with the plant of 1926.

Mr. ADAMS: I don't mean that. As you stated on direct examination, you paid Mr. Lord a certain amount for his share of the plant and equipment of E. J. Lord, Limited, and he was to get 60 per cent. of the profits from the contracts then in existence?

A. Yes, we couldn't arrive at the profit until the job was completed. That's the idea.

Mr. ADAMS: The plant, as I noticed in the minutes of one of the meetings, December 5, 1930, Mr. Lord estimated his own holding, as it were, in the remaining portion of the plant was \$12,000. and you compromised by paying him \$3500.?

A. Yes. [153]

Q. So you did place a value on that plant for which you reimbursed the company?

A. Yes, the plant was valued at something all the time, and the plant Mr. Lord had Mr. Williams appraised, which we thought was high. We worked on the general contractors' schedule, and we had Mr. Grainger of the Iron Works appraise it, and this was worked out as a compromise.

Mr. KAY: What officer of your company has been in charge of tax matters, making returns and so forth?

(Testimony of E. E. Black.)

A. Mr. MacComisky makes out the tax returns, working with Mr. Buchholtz. That is left up to them. They talk to me and tell me what they have done.

Mr. KAY: You will admit as a matter of record that you are representing E. E. Black, Limited?

Mr. PETERS: Yes, I am representing E. E. Black, Limited.

Mr. KAY: And E. E. Black, Limited, under the agreement with E. J. Lord, would be liable for forty per cent. of any Territorial taxes that would have to be paid in this appeal as a result of these proceedings?

A. Yes.

Mr. WRENN: We rest, subject to our right to reexamine Mr. Buchholtz after his further cross-examination.

Mr. KAY: May it please the Board, we would like [154] this matter to go over pending our examination of these documents and other data that have been introduced in evidence. As I stated to the Board this morning, evidently there was a misunderstanding as to this case going on this morning, and consequently we haven't made preparations.

(Adjourned tentatively to Wednesday, December 9, 1931, at 9 a. m. [155])

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Satur-

day, December 12, 1931, at 10:25 o'clock a. m., all members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

Mr. KAY: We offer on behalf of the Tax Assessor taxpayer's trial balances for the months November and December, of 1929, and for the months of the year 1930, including January to December, inclusive. These trial balances are photostatic copies furnished by the taxpayer as abstracts from the books of the company.

(Document offered in evidence received and marked "Tax Assessor's Exhibit B1 to B14" inclusive.)*

Mr. PETERS: We have no objection unless it is the contention of the Government that these go to show different figures than we have contended, the distribution to Mr. Lord of profits and surplus account. We do not see the materiality. If counsel [156] says in his statement to us that he wants to round out the picture, and get everything before it, that is all right, but we want to know if it shows any different set-up than we contend for. That is the original sixty thousand dollar capital contributed by Mr. Lord and undivided profits carried in the surplus account. If it does, we should certainly like to amend our set-up, because we do not contend for anything different than the distribution of sixty thousand dollars in capital and the balance in surplus and undivided profits, and if there are

*Omitted from printed record on stipulation by counsel.

any figures that change that, that counsel in argument or otherwise after the case closes contends is incorrect, as a matter of computation, we should like to know it now; because our desire is to go to this board practically on an agreed state of facts. We do not believe there is any room for any argument or any disagreement between the Government and ourselves on the facts. As far as the application of those facts to the law is concerned, that is a matter, of course, on which we are going to disagree and on which the Board has to decide, but we do not want this Board to have any disagreement as to the facts, and if counsel's argument will show any different set-up than the evidence of Mr. Camp, we should like to know it.

Mr. KAY: Counsel is going to the very issues when [157] he asks to be informed as to what we intend by the introduction of these particular exhibits. The Board will recall counsel has offered on behalf of the taxpayer excerpts from the company's books, E. J. Lord, Limited, and E. E. Black, Limited, and in offering those excerpts they have taken those piecemeal, and they feel it sets out the picture according to what they think is helpful to them and their contentions. We think we should fill out the picture and bring to this Board all parts of the books of the company. That will give to the Board the entire picture. I might state that carried under assets in these trial balances are the item "Treasury stock, \$273,853." and right on through these trial balances will be found that entry. The Board is familiar with our position, to-wit, that

the transaction involved here was not a transaction in the nature of distribution of dividends by E. J. Lord, Limited, but an out and out sale of stock by E. J. Lord to E. J. Lord, Limited, and, consequently, in support of our contentions, we offer this particular exhibit. I think it is relevant and goes to show the set-up as it actually was.

Mr. PETERS: With that understanding, whatever consolation counsel gets out of the fact that in the interim between December 13, 1929, and February or March, 1931, when the redemption was finally [158] consummated, whatever consolation counsel gets out of that he is entirely welcome to. I might say to the Board on this question of an out-and-out sale of stock the Board must bear in mind we do not contend there was not a sale of stock. Our contention is that every voluntary redemption of stock involves two elements. The first step in the voluntary redemption of stock is the purchase of the stock that is desired to be redeemed, and the second step is the retirement of that stock, either in the possession of a corporation or in the possession of outside parties. When stock comes into a corporation with the idea of retaining it, it is an out and out purchase. When it is bought with the purpose of redeeming it it is an out and out purchase. You cannot have a voluntary redemption without a purchase, whether that purchase be for cash alone or whether it be part cash and part specie or the transfer of assets belonging to a corporation represented by the value of the purchased stock. We have never contended that as far as the first step is concerned in the process of the inten-

tion of the corporation to redeem its stock,—we have never contended that the first step was not a purchase, but we have said the character of that act, its legal effect, was reflected by the intention of the parties. That is the reason for the evidence of Mr. Buchholtz, the evidence of myself, [159] and the evidence of Mr. Black,—to show the intentions. The mere fact that there was a purchase does not mean anything. It is the intention with which it was done. A deed may be a mortgage, a loan may be a conditional sale, a mortgage may be a conditional sale, it all depends on the intention of the parties when the original agreements are entered into. I do not want to go into the merits of this thing at the present time. The Board is going to have sufficient when we argue this out, but I do not want the Board to get any erroneous idea as to the situation as stated by counsel. We have two methods of retirement of stock. One is a voluntary method and the other is involuntary. That voluntary retirement may involve one holder of stock. You cannot proceed to the redemption of that stock unless the corporation acquires it. If it acquires it for the purpose of redemption that is one thing; if it acquires it for the purpose of selling it again, putting it out in the hands of other parties, of course that is a purchase of stock, just as if it would purchase the stock of any corporation, hold it and pass it on for value, but, if the corporation is purchasing it for redemption, it must buy it. It cannot take it away involuntarily. It can say everyone shall produce and hand to the corporation ten or

twenty per cent. of its stock, for which they shall have paid part, plus the [160] undivided profits or surplus, so it is the intention with which they go into it in the first instance. If it is a question of involuntary retirement, the stockholder has no volition in the matters, according to the by-laws. Just as soon as there is a voluntary redemption of stock resulting from an agreement between the corporation and individual stockholder or stockholders it is a question of intention. If there is anything that is incorrect so far as we are concerned in the matter of figures we want to make it correct.

The CHAIRMAN: Objection overruled.

(Document offered in evidence received and marked: "Tax Assessor's Exhibit B.")*

Mr. KAY: We offer next copy of the investment account taken from the books of E. J. Lord, Limited, or E. E. Black, Limited, and likewise a copy of the stock account taken from the same source, and ask that the same be marked.

Mr. PETERS: Subject to our checking, so there be no inaccuracies.

Mr. WRENN: We understand this heading is not taken from the books. We would like to have you lay the foundation before introducing it.

Mr. KAY: Mr. Glass informs me those headings are explanatory notes, but the items are all exact copies of the items appearing in the books. [161]

(Documents offered in evidence received and marked: "Tax Assessor's Exhibit C" and "Tax Assessor's Exhibit D.")

*Omitted from printed record on stipulation by counsel.

TAX ASSESSOR'S EXHIBIT C
E. J. LORD, LIMITED OR E. E. BLACK, LIMITED
BOOKS OF ACCOUNT

Securities Purchased, also Securities Received in Payment of Contracts,
 by E. J. Lord, Limited, and Successors.

Date	Name of Security		Par Value	Amount Paid
Sept. 12, 1927	Lihue Plantation Co.—	Trust Notes	\$10,000.00	\$10,000.00
Sept. 12, 1927	Crown Willamette Paper Co.	Bonds	10,000.00	10,200.00
Sept. 12, 1927	Minnesota Power & Light Co.	Bonds	5,000.00	5,075.00
Sept. 27, 1927	Arkansas Power & Light Co.	Bonds	10,000.00	9,750.00
Sept. 27, 1927	Northern States Power Co.	Bonds	5,000.00	5,200.00
Dec. 17, 1927	Columbia Steel Corp.	Bonds	5,000.00	4,987.50
Dec. 17, 1927	Alabama Power Co.	Bonds	10,000.00	10,425.00
Dec. 17, 1927	Los Angeles Gas & Electric Co.	Bonds	5,000.00	5,150.00
Dec. 17, 1927	Sierra & San Francisco Power	Bonds	5,000.00	5,112.50
Feb. 9, 1928	Appalachian Elec. Power Co.	Bonds	10,000.00	10,075.00
Feb. 9, 1928	Texas Power & Light Co.	Bonds	10,000.00	10,100.00
Feb. 9, 1928	Seattle Lighting Co.	Bonds	15,000.00	14,625.00
May 29, 1928	Emporium Capwell Corp.	Bonds	10,000.00	9,750.00
May 29, 1928	East Bay Water Co.	Bonds	5,000.00	5,037.50
Nov. 2, 1929	Lihue Plantation Co.—	Trust Notes	5,000.00	5,000.00
July 8, 1930	Hawn. Bitumals Co. Stock 40% of \$5000.			2,000.00
Sept. 24, 1930	Hawn. Bitumals Co. Stock 20% of \$5000.			1,000.00
Oct. 30, 1930	60 Shares Theo. H. Davies 7% Pfd.			6,030.00
Dec. 31, 1930	Adjustment of Premium & Discount on bonds disposed of.			337.50
				<u>\$129,855.00</u>
Deduct:				
Dec. 11, 1929	Redeemed—Columbia Steel Corp.	Bonds		5,000.00
	Total amount of bonds given to E. J. Lord in payment of his stock			<u>69,000.00</u>
Dec. 31, 1930	Balance in Investment Account			<u>\$55,855.00</u>
	Notes Receivable—Purchased			
Apr. 20, 1929	Honolulu Iron Works			50,000.00
July 9, 1929	Hawaiian Trust Company			50,000.00
	St. Louis Heights Improvement Bonds			<u>Received in payment of Contract:</u>
Sept. 30, 1929	St. Louis Heights Improv. Bonds		25,000.00	25,000.00
Oct. 31, 1929	St. Louis Heights Improv. Bonds		16,500.00	16,500.00
Nov. 30, 1929	St. Louis Heights Improv. Bonds		25,500.00	25,500.00
Dec. 31, 1929	St. Louis Heights Improv. Bonds		39,000.00	39,000.00
Dec. 31, 1929	St. Louis Heights Improv. Bonds		12,500.00	12,500.00
Jan. 1, 1930	St. Louis Heights Improv. Bonds		19,500.00	19,500.00
				<u>138,000.00</u>
Deduct:				
Sept. 30, 1929	To Honolulu Iron Works—on account Given to E. J. Lord in payment of his stock			19,000.00
				<u>119,000.00</u>
Feb. 28, 1930	St. Louis Heights Improv. Bonds		40,500.00	40,500.00
Apr. 30, 1930	St. Louis Heights Improv. Bonds		60,500.00	60,500.00
Apr. 30, 1930	St. Louis Heights Improv. Bonds		45,000.00	45,000.00
June 30, 1930	St. Louis Heights Improv. Bonds		62,500.00	62,500.00
July 30, 1930	St. Louis Heights Improv. Bonds		5,551.26	5,551.26
				<u>214,051.26</u>

Date	Name of Security	Par Value	Amount Paid
Deduct:			
Mar. 31, 1930	To Theo. H. Davies & Co.—on account	15,000.00	15,000.00
July 31, 1930	Sold to Liberty Bank	50,000.00	49,000.00
	Discount on above sale		1,000.00
July 31, 1930	Given to E. J. Lord in payment of his stock	23,000.00	23,000.00
Dec. 31, 1930	Given to E. J. Lord in payment of his stock	68,000.00	68,000.00
			<hr/> 156,000.00
Dec. 31, 1930	Balance in St. Louis Heights Bond Account		\$58,051.26

Securities and Cash given to E. J. Lord in Payment of his Stock holdings in
E. J. Lord, Limited, Etc.

Date	Name of Security	Par Value	Amount
Feb. 28, 1930	Lihue Plantation Co. Trust Notes	\$10,000.00	\$10,000.00
Dec. 31, 1930	Arkansas Power & Light Co. Bonds	10,000.00	10,000.00
Dec. 31, 1930	Alabama Power Co. Bonds	10,000.00	10,000.00
Dec. 31, 1930	Texas Power & Light Co. Bonds	10,000.00	10,000.00
Feb. 28, 1930	Seattle Lighting Co. Bonds	15,000.00	15,000.00
Dec. 31, 1930	Emporium Capwell Corp. Bonds	9,000.00	9,000.00
Feb. 28, 1930	Lihue Plantation Co. Trust Notes	5,000.00	5,000.00
			<hr/> 69,000.00
Feb. 28, 1930	Honolulu Iron Works		50,000.00
Feb. 28, 1930	Hawaiian Trust Company		50,000.00
Feb. 28, 1930	St. Louis Heights Improv. Bonds	119,000.00	119,000.00
July 31, 1930	St. Louis Heights Improv. Bonds	23,000.00	23,000.00
July 31, 1930	St. Louis Heights Improv. Bonds	68,000.00	68,000.00
July 31, 1930	St. Louis Heights Improv. Bonds		482.36
	Accrued Interest		
Feb. 13, 1930	Cash		1,000.00
July 17, 1930	Cash		373.00
Dec. 26, 1930	Cash		68,313.98
			<hr/> 449,169.34
Dec. 31, 1930	Amount shown in the Treasury Stock Account		
Entry in 1931—for 40% Federal Taxes		26,904.66	
Feb. 28, 1931	To Treasury Stock Account		
Less:			
May 31, 1931	Adjustment—Stock Account	6,576.16	20,328.50
			<hr/> \$469,497.84
Settlement—Interest not charged to Treasury Stock Account—Dec. 31, 1930		\$ 1,277.86	

Note:

Dates and figures shown on this statement were taken from the Books of Account of the Company.

TAX ASSESSOR'S EXHIBIT D
E. J. LORD, LIMITED, OR E. E. BLACK, LIMITED.
Schedule Showing Original and Re-issued Certificate—E. J. Lord, Limited, & Successors—Taken from the records of the Company.

No. of Certificate Original	Re-issued	Date	Name	No. of Shares	Transferred to:	Date	No.	Certificates Surrendered	Shares
No. 1		Sept. 3, 1926	E. J. Lord	800	E. J. Lord & E. E. Black	Nov. 8, 1926	1		800
2		Sept. 3, 1926	E. E. Black	197					
3		Sept. 3, 1926	Geo. Buchholtz	1	E. E. Black	Oct. 1, 1926	3		1
4		Sept. 3, 1926	P. J. Erben	1	E. E. Black	Oct. 1, 1926	4		1
5		Sept. 3, 1926	T. Ikejiri	1	E. E. Black	Oct. 1, 1926	5		1
No. 6		Oct. 1, 1926	E. E. Black	3					
7		Nov. 8, 1926	E. J. Lord	310	Treasury Stock	Feb. 15, 1930	7		310
8		Nov. 8, 1926	E. J. Lord	200	Treasury Stock	Feb. 15, 1930	8		200
9		Nov. 8, 1926	E. J. Lord	90	Treasury Stock	Feb. 15, 1930	9		90
10		Nov. 8, 1926	E. E. Black	200	E. E. Black, etc.	Feb. 15, 1930	10		200
11		Feb. 15, 1930	E. E. Black	196					
12		Feb. 15, 1930	E. J. Lord	1	E. E. Black	Feb. 15, 1930	12		1
13		Feb. 15, 1930	Geo. Buchholtz	1	E. E. Black	Feb. 15, 1930	13		1
14		Feb. 15, 1930	J. P. Erben	1	E. E. Black	Feb. 15, 1930	14		1
15		Feb. 15, 1930	T. Ikejiri	1	E. E. Black	Feb. 15, 1930	15		1
16		Feb. 15, 1930	E. E. Black	4					

[260]

Mr. KAY: We offer letter dated December 19, 1930, rather, copy of letter dated December 19, 1930, addressed to Mr. E. J. Lord, care of Hawaiian Trust Company, Limited, from E. E. Black, Limited, referring to the transaction under subject of inquiry before this Board, a copy is offered as being an exact copy of the letter in the files of E. E. Black, Limited.

Mr. WRENN: Is that letter compared with the original from which it was taken?

Mr. KAY: I will give you a copy and upon subsequent check we shall be glad to correct the same.

Mr. ADAMS: You purport to furnish us a true copy?

Mr. KAY: Yes.

(Document offered in evidence, consisting of three pages, received and marked: "Tax Assessor's Exhibit E.")

TAX ASSESSOR'S EXHIBIT E.

3 Papers.

[Seal]

TERRITORY OF HAWAII
TREASURY DEPARTMENT.
HONOLULU.

December 19, 1930. H. T. K.

Mr. E. J. Lord,
c/o Hawaiian Trust Co., Ltd.,
Honolulu.

Dear Sir:

Enclosed please find in duplicate Auditor's Report, with accompanying Balance Sheet and Statement of Profit and Loss for the period, ending

letter of Mr. L. N. MacComiskey, dated December 17th, 1930, showing Federal and Territorial Taxes computed on the profits of the Contracts in which you have an interest, as in our agreement with you dated December 13th, 1929. We wish to mention here that the Federal Income Tax has been computed at the rate of 12%, as it is practically a certainty that the tax rate will be raised from 11% to 12% for this year's earnings. We will have a document drawn up, stating that in case the tax rate should not be 12% we will reimburse you with the difference, and will hand you the document at the time of settlement.

From the Auditor's Report and Mr. MacComiskey's letter we get the following:

Profits from Contracts: (as specified in Agreement of Dec. 13, 1929)	\$588,039.89
Less:	
Taxes (as computed in Mr. Mac- miskey's letter, Dec. 17, 1930)	95,567.93
Net Profits on above Contracts	<u>\$492,471.96</u>
60% of \$492,471.96, due you	\$295,483.18
Less:	
Paid on account (as per State- ment Dec. 31, 1929)	124,947.06
	<u>170,536.12</u>
Plus:	
Additional for Plant (as agreed)	3,500.00
	<u>\$174,036.12</u>
	<u>[261]</u>

2.

Furthermore, we are liable for 40% of your Federal and Territorial Income Taxes to which you may become liable upon income accrued by reason resulting from the sale of the 600 shares of E. J. Lord to us. This is payable upon assessment, as per agreement of December 13, 1929, and will be paid by us to you, or designated representative at such time as it is due.

We propose to pay you in the following manner, this giving you not more than 60% of the St. Louis Heights Bonds received, and not more than 60% of Industrial Bonds we had in possession in December 1929.

- | | | |
|-----|---|-------------|
| (1) | St. Louis Heights Improvement Bonds at 5%—136 at \$500. with coupons attached from August 15, 1930. | 68,000.00 |
| | (Interest see below) | |
| (2) | Industrial Bonds | \$39,000.00 |
| | 10 Arkansas Power & Light Co., 5½% \$10,000.00 with coupons attached from Oct. 1, 1930. | |
| | (Interest see below) | |
| | 10 Alabama Power Co. 5% 10,000.00 with coupons from Dec. 1, 1930. | |

10	Texas Power & Light Co., 5% with coupons from Nov. 1, 1930.	10,000.00
9	Emporium Cap- well Corporation, 5½% with coupons from Oct. 1930	9,000.00
(3)	Cash	67,036.12
making a total of one hundred seventy- four thousand thirty-six 12/100 dollars		<u>\$174,036.12</u>

We also propose to pay to you the sum of \$607.50 being interest on above bonds from August 1st, 1930, in lieu of interest coupons computed as follows:

St. Louis Heights Impr. Bonds—	
½ month at 5%	\$141.67
Arkansas Power & Light Co.—	
2 months at 5½%	91.66
Alabama Power Co.—	
4 months at 5%	166.67
Forward—	\$400.00
	[262]
Bro't Forward	\$400.00
Texas Power & Light Co.—	
3 months at 5%	125.00
Emporium Capwell Corp.—	
2 months at 5½%	82.50
	<u>\$607.50</u>

Trusting this will meet with your approval and awaiting a reply what day will be suitable to make the settlement, we remain,

Very truly yours,

E. E. BLACK, LIMITED,

By.....

Treasurer.

[263]

HENRY GLASS

was duly called and sworn as a witness for the Tax Assessor, and testified as follows:

Direct Examination by Harold T. Kay, Esq.

Q. State your name and occupation?

A. Henry Glass.

Q. Your occupation? [162]

A. Income Tax Assessor, Territory of Hawaii.

Q. You are income tax assessor for the Territory of Hawaii?

A. Yes.

Q. For how long have you served in that capacity?

A. Since January 1928.

Q. Was there any income tax return filed by E. J. Lord for the year 1930?

A. Yes.

Q. When was that filed?

A. The return was filed March 2, 1931.

Q. By whom?

A. By the Hawaiian Trust Company, account of E. J. Lord.

(Testimony of Henry Glass.)

Q. Will you state whether that return is in the record here or a copy thereof?

A. There is a copy.

Q. What does that return show?

A. Gross income, \$527,598.20; deductions, \$534,543.78; deficit \$6,945.58.

Q. Mr. WRENN: Is there any point that this is not correct?

Mr. KAY: That is part of the record.

Mr. ADAMS: It came up to us on appeal.

Q. What else does it show?

A. Exemption of \$1400., personal exemption.

Q. How is the sale of stock by E. J. Lord to E. J. Lord, Limited, reflected? [163]

A. Under item 8, dividends from corporations subject to Territorial income tax, an item E. J. Lord, Limited, \$512,838.54. That was supposed to be—

Mr. PETERS: I object to what it was supposed to be.

Q. Is there any other reference to that?

A. Item 8 refers back to Schedule B.

Q. What does Schedule B show?

A. Schedule B shows profit from sale of real estate, stocks, bonds, and so forth. That is the heading of Schedule B and under the items it says "Kind of property, stocks. Date acquired, 1926; date redeemed, 1930; redemption \$60,000."

Q. Anything else shown?

A. Cost price sixty thousand dollars; net profit none.

(Testimony of Henry Glass.)

Q. What is the total of that schedule?

A. Profit from sale of real estate, stocks, bonds and so forth. And there is another memo, redemption sale of 600 shares of E. J. Lord, Limited. It says here in one of the columns, the column is printed: "Selling price" and the words "selling price" seems to have been attempted to be ruled out, and the word "redemption" put on top of it. We have no such word in any Territorial Income Tax law.

Mr. ADAMS: Do those words refer to an item of the schedule?

A. Schedule "B" is used, should be put under item 5. It would naturally go there. Schedule "B" would [164] naturally go under item 5. I don't know why they put it in that way. It does go under the last column of schedule "B." It shows "net profit, none" so of course there would be "none" under column 5, but they show here \$512,838.54.

Q. Was there any taxable income shown by that return?

A. None.

Q. Any deficit?

A. Deficit 6945.59.

Q. The examination of that return, did your office make an examination of the books of E. J. Lord, Limited?

A. To a certain extent.

Q. And as a result of that examination what action was taken by your office?

(Testimony of Henry Glass.)

A. I found there was a sale of stock in our opinion by E. J. Lord, and we decided to assess on the profit that he had derived from the sale of stock.

Q. Was such an assessment made?

A. Yes, sir.

Q. What was the amount of that assessment, handing you copy of proposed change in assessment of income tax return of E. J. Lord? Will you refresh your memory?

A. We sent them as required by law notice of proposed change in assessment on income tax return, dated May 14, 1931.

Mr. PETERS: That was sent by registered mail? [165]

A. By registered mail.

Mr. PETERS: And you have the receipts for it?

A. Yes.

Q. Give the details?

A. Gross income, first return, \$527,598.20; deductions, first return, 534,543.78; exemptions, \$1400. In the next column, as changed, gross income, 430,833.66; deductions 21,705.24; exemptions \$1400.; net taxable income \$407,728.42; tax 19,161.42.

Q. What was done in respect to that assessment by Hawaiian Trust Company or E. J. Lord?

A. Nothing that I know of.

Q. Subsequently did Hawaiian Trust Company file on behalf of E. J. Lord an amended return?

A. Yes.

(Testimony of Henry Glass.)

Q. Referring to the record, will you state whether that amended return is part of the record?

A. Yes.

Mr. WALSH: Yes, what?

Q. Is that return part of the record?

A. It is.

Q. What date was that filed with the income tax bureau?

A. January 18, 1931.

Q. Who delivered it to your office?

A. By Mr. Camp.

Q. What does that return show?

A. Gross income, \$421,329.64; gross deductions, [166] 428,275.22; deficit 6,945.58. You want the details of the income and deductions?

Q. Yes?

A. Income, item 3, 9969.99.

Mr. WRENN: Isn't the return the best evidence?

Mr. KAY: Yes, but it is explanatory.

A. (Continuing) Item 8, dividends from corporations subject to Territorial income tax, Pioneer Mill Company, \$580.; Maui Agricultural, \$1308.; E. J. Lord, Limited, \$406,569.98. (See schedule.) A total of 408,547.98; item 8b, 2901.67; deductions: Interest,—

Q. Passing from deductions to the reverse of the income return, will you state what is shown on Schedule "B" entitled "profit from sale of real estate, stock, bonds, and so forth?"

(Testimony of Henry Glass.)

A. Schedule "B" should be the profit from sale of real estate, stock, bonds, and so forth, but the word "sale" has been obliterated and the word "redemption" put on top of it, and the item "Kind of property"—

Q. Do these same items appear in respect to this return under Schedule "B" as appear in the first return?

A. Yes, only they do not put in item under redemption column. There is no redemption column in our return. They have scored the selling column out. Let me [167] give the items of Schedule "B." "Kind of property, 600 shares of E. J. Lord, Limited. Date acquired; 1926. "Date sold, it should be, but the word "sold" is obliterated and the word "redeemed" put in its place,—"1930; cost price sixty thousand dollars; net profit, none."

Q. Was an assessment made in respect to that amended return by your office?

A. Yes.

Q. Will you state what is the date of that assessment and what the assessment was?

A. June 19, 1931, as returned gross income 527,598.20; deductions, 534,543.78; exemptions, \$1400. As changed: Gross income, 421,329.64; deductions, 21,705.24; exemptions 1400.; net taxable income, 398,224.40; tax, 18,686.22.

Q. To whom was that notice of assessment delivered?

A. To Mr. Carter Galt of the Hawaiian Trust Company.

(Testimony of Henry Glass.)

Q. By whom?

A. By me.

Q. On what date?

A. On June 19th.

Q. And that was the day after you received the amended return, was it?

A. Yes.

Q. Can you state from your own knowledge whether the appeal now pending before this Board was filed prior to or after the filing of the amended return [168] and assessment made by you?

A. I don't recall.

Q. Was it before or after?

A. It was after the assessment was made, because the—

Mr. PETERS: It was after the amended assessment?

A. Yes, the assessment dated June 19th. The Hawaiian Trust Company rang me up. I think it was Mr. Camp, after he had filed the amended return on June 18th, and requested that a notification be given him the next day, if possible, of the assessment we intended to make. I assured him at that time I couldn't possibly verify the existing figures in a day. So I thought it over, however, and the next morning I thought we will cancel the original assessment and we will make an assessment based on this amended return of June 18th and hand it to him, as he said their lawyers wanted to appear immediately, so just to be sure it got

(Testimony of Henry Glass.)

into the proper hands, I got them to make out the notice and took it down myself and delivered it myself to Mr. Carter Galt.

Q. Carter Galt is an officer of the Hawaiian Trust Company?

A. I believe he is.

Q. And the original assessment against the first return was cancelled?

A. That cancelled that.

Q. And the appeal before this Board relates to the part on the amended return? [169]

A. This \$18,000. tax which we assessed.

Q. Your staff has made an examination of the books of E. J. Lord, Limited?

A. We have made a partial examination to satisfy ourselves on this.

Q. As a result of that examination what conclusion did your department reach and did you reach as Assessor in respect to the contention made by the Taxpayer that the payment made by E. J. Lord, Limited, to E. J. Lord for the 600 shares of stock was simply a dividend and was not a payment as and for the purchase of stock?

A. We thought it was a sale of stock, just like any other sale of stock. The question of whether the purchaser gets the money and what he intends to do with the stock after he buys it is not a question for the Government. The purchaser may claim a loss on the sale of the stock or he may make a gain on the sale of his stock. The government does not inquire into the question where the purchaser

(Testimony of Henry Glass.)

of the stock got the money or what he is going to do with the money. The assessment was made against E. J. Lord because he had sold his stock in the corporation. Did you say something about dividends?

Q. Did you find from the books of E. J. Lord, Limited, that a dividend in the amount paid to E. J. Lord had ever been declared?

A. No, there was no dividend declared. [170]

Q. There was not?

A. We examined the minutes about that, and it is impossible that a dividend could be declared to one stockholder, that is against the law, and the books of account December 31st would not support any suggestion of dividend because the books of account to December 31st of E. J. Lord, Limited, and E. E. Black, Limited, showed that the stock was carried in the Treasury stock account. There was no suggestion of a dividend at all even in the books of account of the company.

Q. Did you find appearing in the books of account and other records of the company the expression: "Sale of stock by E. J. Lord and purchase by E. J. Lord, Limited"?

A. They had a supplement account in their books of account of the corporation, E. J. Lord, Limited, and E. E. Black, which spoke of cash and securities being handed to E. J. Lord for the purchase of his stock, 600 shares.

Q. In determining the taxability of gains resulting from the sale of stock did you have occasion

(Testimony of Henry Glass.)

to refer to any of the provisions of our statutes which throw enlightenment upon the matter?

A. Our law is very clear and very specific. It definitely states that income includes gains, profits and income derived from sales of moveable property, [171] less the cost of purchasing and producing the same. These are almost the actual words in the Statute?

Q. That provision occurs in the income tax statute?

A. Yes, I think it is 1390, the Territorial income tax law taxes two separate and distinct gains.

Mr. ADAMS: To save time, here is 1390.

A. Yes, section 1390, I quoted just now. The Territorial Income Tax law.

Mr. WRENN: Just what question are you answering now?

A. The provisions of the law.

Mr. KAY: The provisions of law he had to refer to in arriving at his decision that this was a taxable gain.

The WITNESS: The Territorial income tax law taxes two separate and distinct gains: A gain arising from the operations of a corporation, and the use of its property; and, secondly, any gain there may be from a sale or disposition of its property.

Q. You said a corporation. Does that likewise apply to individuals?

A. Likewise applies to an individual if he is carrying on a business. And the second point applies both to individuals who are not carrying on a

(Testimony of Henry Glass.)

business and to corporations. That second point is popularly called "Capital loss". Our laws are committed to that just the same as the Federal government. It is well understood. Taxpayer's [172] in this community will understand it.

Mr. WRENN: Objected to as a conclusion of the witness.

Mr. KAY: This witness has a right to testify as to the contemporaneous understand of the community.

Mr. WRENN: I urge my objection as a mere conclusion of the witness.

Mr. KAY: I think it is quite common to show contemporaneous construction. The administration of the statute by the tax officials is charged with the duty of administering.

The CHAIRMAN: Objection overruled.

Mr. ADAMS: I think he can testify as to the practice and whether or not he has been collecting from the public in general.

Mr. KAY: I think that is what he is saying.

Mr. PETERS: If it is the understanding in cases of redemption, voluntary redemption of stock. Apparently Mr. Glass makes no distinction between the purchase by the corporation of its outstanding stock for the purposes of reselling and the purchase for purpose of redemption. I think this is all an explanation to the Board as to how we arrived at it. I haven't objected because I thought the Board would like to see how he arrives at his conclusion, get his mental processes. [173]

(Testimony of Henry Glass.)

Mr. ADAMS: If it illustrates his practice, I should think it should be given.

Mr. PETERS: Let it be understood that the practice as to mere sales or purchase by the corporation of its own stock, or in cases of redemption, there might be a distinction in the practice.

Q. What has been the practice in the past followed by your office in respect to the taxation of gains resulting from the sales of stock?

Mr. PETERS: Objected to as immaterial unless it appears they are gains resulting from sale of stock. There are instances where the sale of stock is made to a corporation under agreement of redemption and purpose of redemption by the corporation.

Mr. ADAMS: I think that will all come out in the answer.

A. The practice has been to tax any gains under the appropriate rate under the Territorial income tax law, and also to allow the taxpayer to deduct any sustained loss on disposition of his stockholdings in a corporation.

Q. Is there any provision in the Territorial income tax law or has there been any practice followed by your department recognizing a redemption of stock as such or a liquidating dividend as such?

Mr. WRENN: Objected to as more than duplicitous, and it is incompetent, irrelevant and immaterial unless [174] it shows the department has dealt with the question of liquidating dividend. Let's find out if he has dealt with liquidating dividend.

(Testimony of Henry Glass.)

business and to corporations. That second point is popularly called "Capital loss". Our laws are committed to that just the same as the Federal government. It is well understood. Taxpayer's [172] in this community will understand it.

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Mr. PETERS: If it is the understanding in cases of redemption, voluntary redemption of stock. Apparently Mr. Glass makes no distinction between the purchase by the corporation of its outstanding stock for the purposes of reselling and the purchase for purpose of redemption. I think this is all an explanation to the Board as to how we arrived at it. I haven't objected because I thought the Board would like to see how he arrives at his conclusion, get his mental processes. [173]

(Testimony of Henry Glass.)

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Q. What has been the practice in the past followed by your office in respect to the taxation of gains resulting from the sales of stock?

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Mr. ADAMS: I think that will all come out in the answer.

A. The practice has been to tax any gains under the appropriate rate under the Territorial income tax law, and also to allow the taxpayer to deduct any sustained loss on disposition of his stockholdings in a corporation.

Q. Is there any provision in the Territorial income tax law or has there been any practice followed by your department recognizing a redemption of stock as such or a liquidating dividend as such?

Mr. WRENN: Objected to as more than duplicitous, and it is incompetent, irrelevant and immaterial unless [174] it shows the department has dealt with the question of liquidating dividend. Let's find out if he has dealt with liquidating dividend.

(Testimony of Henry Glass.)

Mr. ADAMS: That can all be brought out.

The CHAIRMAN: Objection overruled.

A. There is no such term as "redemption of stock" in our Territorial income tax law, nor in the corporation law, as far as I have seen. Neither is there such a term as "liquidating dividend" either in the Territorial income tax law or in any other law of the Territory of Hawaii. There is a section in our law which deals with retiring or reducing a number of shares by distributing among its stockholders who may be entitled to the distribution any assets of the corporation not in excess of the value of the remaining shares of the corporation which are not so required. I think you will find that in section 3351, revised laws, 1925. The term "liquidating dividend" is a term used in the Federal internal revenue acts. There is no corresponding term in our law; therefore, we do not know what anyone is talking about when they are talking about liquidating dividend, as far as my business is concerned in applying the Territorial income tax law.

Mr. ADAMS: I don't think he has answered your question. You asked him "What has been his practice." [175]

Q. Will you make that a little bit clearer, the matter of practice?

(Question read by the reporter as follows:

"Is there any provision in the Territorial income tax law or has there been any practice followed by your department recognizing a redemption of stock as such or a liquidating dividend as such?")

(Testimony of Henry Glass.)

A. Well, the Territorial income tax bureau cannot apply Territorial income tax law on a question of redemption of stock, because there is no such term in our law.

Q. As a matter of practice has your department taxed all gains resulting from sales of stock in a corporation?

A. Yes, sir; we assess the man that sold, not the man who bought.

Mr. ADAMS: Has there been any practice in regard to the redemption of stock by your department, either redemption of stock or liquidating dividend? Has there been any practice.

A. I cannot answer "yes" or "no." There is no such word as "liquidating dividend" or "redemption." Consequently when you ask me about a liquidating dividend, there is nothing in our law about it.

Mr. ADAMS: We are trying to get the facts.

A. In a similar situation if a stockholder were [176] to offer his holdings, if his ownership of a part of the corporation was bought by the other stockholders, or by whomsoever, it is a sale of stock as far as the Territory is concerned. As far as we know it is a sale of stock. I am talking about the seller. To him it is a sale of stock, and if he gets more than he paid for it, it is a taxable gain under the Territorial income tax law.

Q. And it has been your practice to tax those gains in the past?

A. Yes.

Q. Suppose there has been a redemption of stock, how would you handle it?

A. As far as I know, it is a sale of stock to him.

Q. Can you give us any specific instance?

A. I can't give you any specific instance at the moment. That very seldom happens.

Mr. ADAMS: If there has been any redemption of stock you have handled it, as far as the man whose stock has been redeemed, as a sale of stock on his part?

A. I would naturally do that, handle it that way, if any such thing arises.

Q. You know of no such thing in the past where it has been handled otherwise?

A. No, I don't.

Mr. ADAMS: Has there been any transfer of stock corresponding to such a transaction in the past that has been [177] handled by your department?

A. As I say, I can't give any specific instance. If you ask me today that I will try to look back in the files and probably between us we could look up something like that to find it out, but it is not a thing I can answer yes or no right away. I have two or three instances in my mind, but I would certainly have to look them up to find out what was done first.

Q. It is the contention in this case that the payment made by E. J. Lord, Limited, to E. J. Lord was a dividend of the character that is granted an exemption under the provisions of Section 1391,

(Testimony of Henry Glass.)

Revised Laws, 1925, reading that dividends paid on stock owned on which corporations have paid a two per cent. tax will be exempt. Will you state as a matter of administration of your department whether or what character of dividends therein exempted has been given exemption, and how your department has construed that particular term "dividend" as used in that provision?

A. We naturally refer to the law in that case, and under our law, under the laws of the Territory, "Dividend" is a distribution of profits arising from the business of the corporation. You will find that outlined in Section 3361. That interpretation of the word "dividend" is the accounting interpretation. When an accountant talks about dividends [178] he talks about a distribution of profits which can only be declared by the directors of a corporation and that is the meaning of the word dividend.

Mr. PETERS: That doesn't say so in the Statute. It doesn't say it can only be declared by a dividend in that section.

A. I didn't say so in that section.

Mr. WRENN: That is your idea of what the law is, is it?

Mr. KAY: Just a moment. The witness is on direct examination and you are not required to answer these questions.

Q. The dividend is a matter of practice, the dividend contemplated by section 1391 which is entitled to exemption is the dividend that has been

(Testimony of Henry Glass.)

duly declared by a corporation as a dividend from profits in those cases where the corporation has paid a tax of two per cent.

Mr. WRENN: Objected to as incompetent, irrelevant and immaterial, not shown that the other situation has ever been presented to the Board.

The CHAIRMAN: Objection overruled.

A. Yes.

Q. In the administration of your department have you ever had occasion to grant exemption or has an exemption been granted in respect to the dividend that was only declared to one stockholder and not declared to all stockholders pro rata? [179]

A. Never that I knew of.

Q. Can you state whether "dividend" as construed by your department, constitutes or consists of a dividend from profits duly declared by a corporation to its stockholders pro rata?

A. Yes, sir.

Q. That is what you understand "dividend" to mean as used in Section 1390?

A. Yes, sir.

Q. In respect to that exemption as granted in Section 1391 can you state whether or not there was any significant fact appearing in the transaction between E. J. Lord and E. J. Lord, Limited, which clearly takes it from that exemption, the particular transaction. I am referring particularly to the surrender of the stock by E. J. Lord. How can that be resold with the provisions of 1391.

(Testimony of Henry Glass.)

Mr. PETERS: Objected to as unintelligible, argumentative, duplicitous, and asking for a conclusion of the witness as to an interpretation of the section of the law.

Mr. KAY: I will reframe it.

Q. Referring to section 1391 it is "provided further that in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has been assessed." In the case before the Board and [180] in the facts thus far adduced in your opinion can it possibly be said that this payment could have been a dividend upon the stock owned of E. J. Lord, Limited?

Mr. WRENN: Objected to as calling for a conclusion of the witness on a question of law.

Mr. ADAMS: Not a question of law, but in the practice of the Assessor's department.

Mr. WRENN: There appears to be no practice. How could he go into that?

Mr. ADAMS: Will you form your question again, to make it the practice of his department.

Q. In the administration of your department and the construction followed by your department in the last proviso in Section 1391, will you state whether it has been the practice to consider payments from corporations as dividends when issued to a stockholder by virtue of ownership of stock?

A. Yes, sir; that always would be considered dividends, and that was the practice of the office

(Testimony of Henry Glass.)

to allow dividends which have been paid by corporations which had been assessed under the Territorial income tax law to be exempt from taxation themselves.

Q. Is a surrender of stock in consideration of the payment, could that possibly as a matter of administration be construed as a dividend?

Mr. WRENN: Objected to as calling for a conclusion of the witness and a conclusion of law. [181]

Mr. ADAMS: I think that is all right. It is a matter of administration. His department administers the law.

The CHAIRMAN: Objection overruled.

A. Of course it is not a dividend because when the corporation pays a dividend the stockholder does not relinquish the stock. We cannot consider the question at all. There is a difference between the stockholder getting his dividend and the stockholder disposing of his holdings; they are two entirely different things.

Q. Have you had occasion to refer to that provision of law providing that shares of stock of a corporation shall be considered as personal property?

A. Yes, we have all those things in our mind. The law distinctly states that shares in a corporation are personal property.

(Adjourned subject to call.) [182]

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Monday, December 28, 1931, at 2 o'clock p. m., all members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

HENRY GLASS,

a witness for the Tax Assessor, resumed the stand and testified as follows:

Cross Examination by Emil C. Peters, Esq.

Q. Just by way of resume, is there any case that you can remember in the Tax Office in which there has been a voluntary reduction of stock?

A. Why do you mean by "a voluntary reduction of stock?"

Q. A redemption of stock as between the corporation and the stockholder, voluntarily entered into between each of them. Do I make myself plain?

A. Yes, but you didn't say what you meant by "voluntary." On the part of the stockholder? [183]

Q. Perhaps I can explain it this way. We are both agreed that the directors are the managers of the corporation?

A. The directors are the directors of the corporation.

Q. The directors are the managers of the corporation?

A. The statute says directors or managers. I assume that is what is meant.

(Testimony of Henry Glass.)

Q. And there is the superior control of the stockholders?

A. Yes, they own the corporation.

Q. There is a superior control of the stockholders?

A. Control in what way?

Q. Of the business of the corporation?

A. The stockholders own the corporation.

Q. Well, they control the business of the corporation? They are superior to the directors, are they not?

A. That is a question of law. I would like to have you decide that for yourself.

Q. I don't want to quarrel with you. You are asking me for a definition and I am trying to give it to you. You do know,—don't you know, that sometimes in the directors and sometimes in the stockholders is reposed the power of reducing the number of shares of capital stock?

A. I think, according to our law, I think it is [184] the stockholders that have the power to reduce the capital. Might we have the revised laws of 1925?

Q. Don't let's bother about that.

A. I would like to have it when I am answering questions along that line.

Mr. KAY: I think the witness has the right to refer to it if he wants to. (Handing copy of the revised laws to the witness.)

The WITNESS: (Witness refers to copy of revised laws) You said reduction of capital? It gives it in section 3351.

(Testimony of Henry Glass.)

Q. You wanted to refresh your recollection. The proposition is that under that Statute a certain percentage of the stockholders regularly assembled can reduce the capital stock, can they not?

A. That is what the section says.

Q. And whether you are a dissenter or not, if the required number of stockholders so vote you have to give up your proportionate holdings in the corporation, would you not, in order to arrive at that reduction?

A. That is a question of law that can all be threshed out in there.

Q. Do you know that?

A. I will give no answer to that.

Q. You are asking me for a definition. I am trying to help you give that definition. Won't you please [185] approach this subject with me in a spirit of friendliness instead of antagonism?

A. Certainly. There is no antagonism.

Q. May it not be so that although a member of a corporation may not be willing to give up his holdings in a corporation, that unwilling member may be forced to by the stockholders in a meeting,—be forced to give up a certain proportion of his stock?

Mr. KAY: Objected to as not proper cross-examination. The witness did not go into the matter of the reduction of stock.

Mr. PETERS: I think we can progress a little more rapidly if we have a little more cooperation from the witness. My position here is a very simple

(Testimony of Henry Glass.)

one. We have a provision for the reduction of the capital stock of a corporation, and that reduction may be accomplished, as you know, by the necessity of the stockholders giving up a certain proportion of their shares; whereas they might hold 100 shares, but, after a 50 per cent. reduction, they would hold 50 shares, and 50 shares would be redeemed. So if we had a 50% reduction and we were stockholders and not be willing to do that, and might vote against it, but by virtue of the fact that the stockholders in regular meeting assembled voted for it, we would have to give up our proportion. That is known as an involuntary method of capital [186] reduction. Now we have certain voluntary methods. The corporation comes to me, like it came to E. J. Lord in this case, and says "We would like to reduce our stock by the holdings which you have at the present time, and that stockholder is not coerced by any provision of the Statute making him give up half of the stock or all of the stock; he voluntarily agrees and assists the corporation in reducing its stock by selling it his stock. And the corporation having acquired it for the purpose of redemption retires it and applies to the Treasurer of the Territory for a reduction of the capital stock. What I want to know is this,—does the witness remember any voluntary reduction of stock as having occurred in the tax office. He comes back with the proposition "What do you mean by 'voluntary,' " and immediately I attempt to define what I mean by "voluntary" and the battle is on.

(Testimony of Henry Glass.)

Mr. KAY: May it please the Board, what Judge Peters has said is a matter of law. If Judge Peters wants to frame his question in the light of argument, what he means by "voluntary reduction" and asks—

Mr. PETERS: Oh, I will withdraw the question.

Q. Do you know of any similar instance in the tax office where the facts are parallel with the instant case, the redemption of Mr. Lord's stock?

A. We have had cases of large losses deducted from income on Territorial income tax returns on liquidation [187] of a company. Would that be something like what you mean?

Q. Are you asking me a question, or are you answering my question?

A. I am answering your question.

Q. Please tell me the names of any companies involving facts similar to the instant case that you have had in that tax office?

A. I don't know anybody that sold 600 shares of E. J. Lord, Limited. I don't know anybody that sold 600 shares of any other corporation, but I do know where a company was liquidated and all of its stock cancelled and the company dissolved and large losses taken off their income tax returns by the stockholders, that may be an analogous case in your mind.

Q. Do you know of any instance in the tax office where the question of taxes has been involved

(Testimony of Henry Glass.)

where an individual has sold his stock in a corporation to the corporation and the corporation has redeemed that stock so purchased?

A. I haven't any in mind just now.

Q. Isn't it a fact that this is the first instance of this kind in your experience in connection with the tax office they have had occasion to meet that?

A. I don't know of any now. I don't remember. I have none in mind now.

Q. All these undivided profits that have been referred to paid taxes, did they not? [188]

A. Which undivided profits do you refer to?

Q. The only ones we have spoken of,—the profits which were paid to Mr. Lord?

A. There were no undivided profits, so far as I know, paid to Mr. Lord.

Q. Haven't we been talking right straight along that the payment to Mr. Lord was composed of sixty thousand dollars of capital originally invested, and the rest was surplus or undivided profits?

A. What was given to Mr. Lord was cash and its equivalent, and you will find on the balance sheet of E. J. Lord, Limited, that that cash and equivalent of cash is carried as the capital of the company, the cash and its working capital and the investments as its temporary investments.

Q. Do you understand that all this time we have been talking about the surplus account and the profits that have gone to that surplus account you haven't considered that as a surplus account?

(Testimony of Henry Glass.)

A. If you will point out the surplus account that you are talking about, I will see whether we considered that a surplus account or not. Are you referring to the surplus account on the books of E. J. Lord, Limited, and E. E. Black, Limited?

Q. What else have we been talking about?

A. Never mind what else we have been talking about. It want to be specific. If that is what you are talking about, there was a surplus on the books of [189] E. J. Lord, Limited, and E. E. Black, Limited.

Q. That surplus had been returned, portions of it had been returned each year and taxes paid on it?

A. I would need to refer to the tax returns to see what taxes had been returned.

Q. They are all in evidence.

A. I assume they are. The amounts shown there I presume were all profits from the activities of the business.

Q. Just answer my question, whether or not this surplus that existed in E. J. Lord, Limited, and E. E. Black, as of the 1st of January 1927, 1928, 1929 and 1930, that the corporation then in existence had paid Territorial income taxes upon?

A. I presume they did.

Q. Can't you say "yes" or "no"?

A. I presume they did.

Q. Can't you say "yes" or "no"?

A. No. You have to examine the books to see that. There may have been exemptions. There may

(Testimony of Henry Glass.)

be items in that surplus that are not taxable under our law.

Q. All the items contained in that surplus that were taxable under the law, income taxes had been paid on it, hadn't they?

A. I presume they were.

Q. If that surplus had been distributed to all the stockholders of E. J. Lord, Limited, and E. E. Black, Limited— [190]

Mr. ADAMS: Why bring in the name of E. E. Black?

The meeting of the stockholders was held on Feby.

~~February~~ 15, 1930, when they voted to disincorporate the company of E. J. Lord, Limited.

Q. This surplus that existed on the 1st of January of 1927, 1928, 1929 and 1930, had it been distributed to all the stockholders of the company at that time, would have been exempt, as far as returned by the individual for income tax purposes, would it not?

A. All dividends payable by Hawaiian corporations that pay 5% taxes on the earnings are exempt under our law?

Q. And if they had been declared as dividends in the previous year or succeeding year a reduction could have been claimed by by the stockholders in the amount they received?

A. I have already stated that dividends to stockholders paid by corporations up to 5% on the net earnings are exempt from taxation on the stockholders return.

(Testimony of Henry Glass.)

Q. So on the 1st day of January, 1930, 1930, this entire surplus could have been distributed to the stockholders then existing and they would have been exempt from any Territorial income tax upon it?

A. I have already answered that question three times.

Q. You have answered it in the affirmative?

A. I have answered that dividends paid to stockholders that have paid the 5% on net earnings are [191] exempt under the Territorial tax laws.

Q. So, if the surplus had been paid as dividends to Mr. Black and the other stockholders, this question would never have arisen? In other words, if Mr. Lord had been paid his sixty thousand dollars and his dividends, this question would never have arisen, would it?

A. They would have been paid the dividend and Mr. Lord would still have held his stock.

Q. If he had been paid sixty thousand dollars for his stock, after all the surplus had been divided, his stock would only be worth sixty thousand dollars?

A. You are going into a lot of suppositions. I don't know what would have happened. I am concerned with facts.

Q. All right, if he had been paid all his share of the profits simply as all other stockholders, and then they had bought his stock for sixty thousand dollars and redeemed it, this question would never have arisen, would it?

A. Would they have had anything to buy stock with after they had paid all that dividend?

(Testimony of Henry Glass.)

Q. Would they not?

A. I don't know.

Q. Suppose they had sixty thousand dollars to pay after they had distributed all of the surplus to all stockholders, and they had bought Mr. Lord's [192] for sixty thousand dollars, and redeemed it, this question never would have arisen, would it?

A. I don't know what would have arisen under supposititious circumstances like that.

Q. Don't you want to answer that question?

A. I have no answer to give to that question except what I am saying.

Q. Take the further supposition that if all the surplus had been distributed in dividends and Mr. Lord's stock had been redeemed for sixty thousand dollars, and the capital stock of the company had been reduced to the value of Mr. Black's stock, and the other three stockholders, this question would not have occurred either, would it?

A. You are making a statement. I don't care to go into that. I have never had that point before,—that point doesn't come up at all on this case.

Q. Take it as a hypothesis?

A. I don't care to.

Mr. PETERS: I would ask that the Board instruct the witness to answer the question. Here is a very simple proposition, so you will understand what I am driving at: According to the evidence 60% of this surplus is turned over to Mr. Lord, plus his original contribution to capital. As far as that

(Testimony of Henry Glass.)

corporation is concerned, they could have distributed the entire surplus existing at that time, could have bought Mr. Lord's stock for sixty thousand [193] dollars. Mr. Black could have turned back his dividend into the corporation and then have gone before the Treasurer's office and reduced the capital of that corporation to the value of Mr. Black's contribution to the 40% of the surplus that he returned.

Mr. WALSH: What is the point of trying to make the witness say that? It seems to me that is an argument before the Board.

Mr. PETERS: As I understood at the last session he was talking about departmental practice, and I am going into departmental practice. I am asking what would have occurred under that hypothetical case down there. I want the Board to understand that if there had been any attempt to evade the payment of taxes, they could have legally have done and accomplished what they did here by distribution of dividends among all those stockholders. Mr. Black could have put his dividend back into the corporation and there would have been no tax assessment under the law, and this question would not have arisen. In other words, it is the tax office which is quibbling here and trying to create a liability which under the circumstances should not exist and never has existed.

Mr. ADAMS: But that is not what has transpired.

Mr. PETERS: We are presenting a hypothetical case, [194] which if we had wanted to go into a lot of red-tape we could have done. Counsel will argue

(Testimony of Henry Glass.)

that dividends must be distributed among all the stockholders. I am trying to show the Board that a dividend by whatever name is a dividend, nevertheless, and to show the Board what we did was not to evade taxes. We did exactly what we could have done by a longer method. We could have declared a dividend of that entire surplus. Instead of that they take a short-cut and they give Mr. Lord his original contribution of capital, and his share of the surplus in the nature of a dividend, and instead of Black taking the dividend that Mr. Lord took and putting it back in the corporation, he takes a short cut and the Territory steps in and says, "You did it that way; the dividend must be to all the stockholders. You can't call that a dividend. A dividend is distributable to all the stockholders according to their holdings" and we are showing by a hypothesis, trying to demonstrate to this Board had we taken the long way around, the red-tape proposition, there would have been no taxation question here at all.

Mr. ADAMS: It seems to me that is a question of argument before the Board. The Tax Assessor's office is bound by the law as it exists.

Mr. PETERS: That's quite true. I thought as Mr. Glass had so learnedly expounded the law and the [195] practice of the Tax Office, I thought that the Board would like to hear what he had to say about this. You would think according to the witness' statement at the last hearing there was a voluntary surrender of stock every day, and yet we haven't an instance of such a thing.

(Testimony of Henry Glass.)

Mr. ADAMS: Why not let it go at that?

Mr. PETERS: All right. It is all right with me. if the Board doesn't want to hear it. That's all I wanted to ask.

Cross Examination by Heaton L. Wrenn, Esq.

Q. As I understand it was in 1928 you first went into the income tax department?

A. That's right.

Q. And you don't intend to qualify here as a lawyer, an expert on corporation law?

A. Oh, no.

Q. You stated in your testimony the other day that it was on March 2, 1931, that the Hawaiian Trust Company, Limited, filed Mr. Lord's income tax return. That was done under a general extension given to the Hawaiian Trust Company?

A. The Hawaiian Trust Company and all its clients.

Q. Prior to the time you became the income tax assessor, what tax experience did you have, Mr. Glass?

A. No particular tax experience. I had made out [196] tax returns at various times, but I have no particular tax experience, no close association with the laws. I had made out Federal taxes.

Q. You made out tax returns occasionally?

A. Yes.

Q. But that was as close as you had ever come to having any experience with tax work?

A. Yes.

(Testimony of Henry Glass.)

Redirect Examination by Harold T. Kay, Esq.

Q. Prior to your appointment as Territorial income tax assessor will you state how many years you had had experience in accounting and keeping of corporation records, books and so forth?

A. Twenty-five years prior to that.

Q. Will you state how many years of the 25 were spent here in the Territory of Hawaii?

A. All of them barring a couple of years in the war service.

Q. Under cross-examination by Judge Peters you refer to dissolutions of corporations where losses were allowed on income tax returns?

A. Yes.

Q. Have you any particular dissolution or dissolutions in mind at this time?

A. We had a very recent one. That was Davies & Company and the Pearl City Fruit Company. Davies & Company were stockholders of the Pearl City Fruit [197] when the assets were liquidated, and Davies & Company as stockholders felt their stock was a loss amounting to about three-quarters of a million dollars, and they deducted from the Territorial income tax returns.

Q. Will you state whether or not Davies & Company were the majority stockholders in the Pearl City Fruit Company?

A. Yes.

Q. As a matter of fact, it owned practically all of the stock in the Pearl City Fruit Company?

(Testimony of Henry Glass.)

A. Yes. There have been a number of other instances of deductions in our Territorial income tax returns by stockholders who have lost money by companies going into liquidation.

HAROLD C. HILL

was duly called and sworn in rebuttal for the Tax Assessor, and testified as follows:

Direct Examination by Harold T. Kay, Esq.

Q. State your name and occupation?

A. Harold C. Hill, tax assessor, First Division.

Q. Territory of Hawaii?

A. Territory of Hawaii?

Q. How long have you held that position?

A. Within a few days of two years.

Q. Appointment as of what date?

A. January 1, 1930. [198]

Q. Prior to that time what was your occupation?

A. For a year and a half collector of internal revenue for the District of Hawaii.

Q. And during that period you were in charge of the administration of the Federal income tax law in the Territory of Hawaii?

A. Yes, sir.

Q. And prior to your appointment as internal revenue collector here in the Territory what position or positions did you hold?

(Testimony of Harold C. Hill.)

A. Approximately three years immediately prior to that time I was income tax assessor for the Territory of Hawaii, and for five years prior to that time I was chief of the division of the income tax collector's office in Honolulu.

Q. You have sat thus far through the hearings in this case?

A. I think I have been present at every session.

Q. You have heard the contention and testimony of the taxpayer's representatives?

A. Yes.

Q. Will you state whether in your opinion the deduction claimed by the taxpayer in this case is a proper deduction under the Territorial income tax law, based upon your experience in administering that law as Territorial income tax assessor?

Mr. PETERS: Objected to as calling for a conclusion of the witness and usurping the functions of this [199] Board.

Mr. KAY: I think it is proper, as the witness has been qualified to express an opinion.

The CHAIRMAN: Objection sustained.

Mr. KAY: May I have an objection to the ruling of the Board sustaining the objection?

Q. In your experience as Territorial income tax assessor will you state whether you recall any deductions such as that claimed by the taxpayer in this case were ever allowed in respect to any Territorial income tax return made by any taxpayer?

(Testimony of Harold C. Hill.)

Mr. PETERS: I object to the question unless it first appears there was a similar case in which the question was raised.

The CHAIRMAN: Objection overruled.

A. I don't recall any such reduction having been made.

Mr. PETERS: Made or claimed or both?

Mr. KAY: I submit if Judge Peters has any questions to ask they may be put on cross-examination.

Q. In your administration as Territorial income tax assessor do you recall whether gains from the sale of stock in corporations were taxed?

A. Yes, they were.

Q. In the Federal income tax law there is a term known as "liquidating dividends" is there not?

Mr. WRENN: Objected to as incompetent, irrelevant and immaterial.

Mr. KAY: That is purely preliminary to show that the [200] Territorial income tax law and Federal income tax law are not similar, particularly as to the term of "liquidating dividends."

Mr. ADAMS: Why don't you ask him a direct question, whether there is any term in the Territorial law similar to the term in the Federal law of "liquidating dividends"?

The CHAIRMAN: Objection overruled.

A. Yes, either in the law itself or in the regulations promulgated by the Commissioner, which have the effect of law.

(Testimony of Harold C. Hill.)

Q. Do you know any similar term in the Territorial income tax law?

A. No I do not.

Q. Will you state whether in your opinion, based upon your administrative experience, both in the Territorial and Federal service, the term "dividend" as used in Section 1391 contemplates or includes the term "liquidating dividend" as that term is generally understood?

Mr. PETERS: Objected to as calling for the conclusion of the witness on a question of law, and usurping the functions of this Board and assuming the fact that there is any understanding in the witness's department as to the meaning of the word "dividend," and an attempt to usurp the functions of this Board, to tell the Board what the meaning of the word [201] "dividend" is.

Mr. KAY: For some reason counsel objects to the Board obtaining the opinions of witnesses as to the administration of the income tax law and in respect to the very matters presented to the Board. We submit the question is entirely proper. If the Board does not care to entertain such evidence, we will defer to the Board's ruling.

Mr. ADAMS: We are not interested in Mr. Hill's opinion. We are interested in the practice of the income tax department of the Territorial tax administration. We assume, and it is proper we should assume so, because the tax administrative officials are presumed to be expert in their line,—

(Testimony of Harold C. Hill.)

we assume they would administrate it according to their interpretation of the law, and they hope to have it sustained in the Courts. His experience, however, in the Federal administration, would have no bearing on his interpreting the Territorial laws. Let's confine ourselves to the practice of the Territorial income tax department.

Mr. KAY: I take it the question will be allowed by deleting the part referring to the Federal service.

(Argument.)

Mr. PETERS: It seems to me counsel confuses his law. We call upon men to testify as to their opinion,—men learned in medicine as to the cause of death, men who by study or observation are skilled in the [202] sciences to give their opinion as to the laws of sciences, and we call men called realtors to give their opinion as to the value of land. Whatever the opinion is, it is finally given by the Court. Suppose that the Court is bothered by the question of Statutory interpretation, would it not be a strange thing to have every attorney in town come and give his opinion as to the Statute. Naturally and properly the Judge would say "Never mind what your opinion is. If you want to argue as to the interpretation of a statute, get appointed as *amicus curiae* or be employed by one of the parties." This Board has first to decide what is the meaning of this word "dividend," and, secondly, whether this distribution was a dividend within

that meaning. Nobody can decide for the Board what is the meaning of that word "dividend" as contained in Section 1391. I am agreed with the Board if there have been any cases of this kind down there and a practice has been followed in disposing of those cases, I think the Board should know, but, if there have been no cases, this witness is not competent to decide.

Mr. ADAMS: Why not ask the witness if in his administration of the Territorial income tax law his department has ever interpreted the word "dividend" as contained in Section 1391 to include what is known in the Federal income tax law as "liquidating dividends"? [203]

Mr. KAY: That is a question of administration. I am now asking a question as to his opinion. I submit he is qualified to express an opinion. However, to meet counsel's objection, perhaps I can reframe this question in such a way that there will be no objection.

Q. If there had ever arisen such a case as is now being presented before this Board, involving a contention that the payment made to Mr. Lord by E. J. Lord, Limited as and for the sale of his stock constituted a liquidating dividend, and, as such, was entitled to be deducted as a dividend under the provisions of Section 1391, would you, as Territorial income tax assessor, have allowed such a deduction?

Mr. PETERS: Objected to as calling for a hypothesis. That is immaterial. That is what this Board is called upon to do. If this question is

(Testimony of Harold C. Hill.)

allowable, why not ask the question "If you, instead of Mr. Glass, had had the duty to determine this matter, what would you have done?"

(Argument.)

Mr. PETERS: My objection is it is not a subject matter of opinion, not a subject matter of expert evidence.

Mr. ADAMS: After all Mr. Hill has been head of the income tax department of the Tax Assessor's office.

The CHAIRMAN: Objection overruled.

Q. (Question read by the reporter.)

A. No, I would not. [204]

Q. You consider the disallowance of the deduction claimed is proper?

Mr. WRENN: Objected to as calling for a conclusion of the witness.

The CHAIRMAN: Objection overruled.

A. Yes, I do.

Q. And that the assessment as made by Mr. Glass is a proper assessment?

A. I believe it to be proper, yes.

Cross-Examination by E. C. Peters, Esq.

Q. Do you know of any case that has occurred in the tax office during your incumbency in which there has been a voluntary reduction of stock of a stockholder of a corporation?

A. I know of a redemption. I don't know whether it is paralled with this case or not. What

(Testimony of Harold C. Hill.)

I have in mind is the Mineral Products Company when they called in their stock and formed the Magnesia Products Company.

Q. That is what I would call an involuntary redemption. Have you finished your answer?

A. I think so.

Q. In the case of the instance which you refer to every stockholder gave up a certain number of shares, or was the par value of the stock reduced?

A. I am speaking from memory on something that happened about 1925 or 1926. As I recall it, I [205] think the stock of the original company, the Mineral Products, was called in and a reduced number of shares in the new company were issued in their stead to those who chose to go on with the company.

Q. In other words, they paid for the redemption of the stock of the Mineral Products with the stock of the newly organized company?

A. You mean the company paid?

Q. You spoke about Mineral Products. I didn't get the name of the second company?

A. Magnesia Products.

Q. The Mineral Products by action of their stockholders reduced their capital stock by retiring a portion of it?

A. Yes.

Q. And then after the reduction or after the amount that still remained did the Magnesia Prod-

(Testimony of Harold C. Hill.)

ucts issue stock to the stockholders of the Mineral Products?

A. Yes, as I recall it, they did.

Q. For the original stock or the redeemed stock. Say, for the sake of argument, I had ten shares of Mineral Products and I was to give up five for the five of Magnesia Products, did I get stock in Magnesia or keep my stock in the Mineral Products and take stock for the five I gave up?

A. I think the Mineral Products went out of the picture. [206]

Q. So, as a matter of fact, it was a complete dissolution and a payment of the stockholders in the old corporation by stock in the new corporation?

A. Yes.

Q. There was no profit involved in that, was there?

A. No, there were plenty of losses.

Q. Let's go back to your statement that according to the income tax statute you would treat this as sales of stock. Gains made by sales of stock were taxed under the income tax law?

A. Yes.

Q. And where a corporation with the intention of redeeming its stock goes out and buys that stock and retires it, would that corporation pay any income tax as a result of that transaction, no matter for what price; can you conceive of the corporation paying any income tax under any state of facts? I would like you to make your own book.

(Testimony of Harold C. Hill.)

Make it any conceivable state of facts by which you can figure up that the acquisition of its own stock by the corporation and its retirement results in a profit to the corporation upon which it would pay any taxes under the Territorial income tax law?

A. I can't draw any situation as that to mind now. I know the Federal government directly states that a corporation cannot either profit or lose by [207] dealing in its own stock, but the Territorial law is entirely silent on that question.

Q. Can you make up any arithmetical problem by which you can compute a profit resulting to a corporation by going out and acquiring its own stock and redeeming it?

A. No, I can't say where there could be any profit.

Q. As a matter of fact, it is not on the cards and it cannot occur. I want to ask you this question: There would have been no objection so far as Mr. Lord and Mr. Black were concerned to claim those as deductions on the ground that the company had already paid the tax, would there?

A. (No answer.)

Q. There are two men that own a corporation and they have three dummy stockholders in order to have a sufficient number of directors under their by-laws. Those two men go to work and figure out that over and above their capital contribution they have a surplus of one hundred thousand dollars

(Testimony of Harold C. Hill.)

profits made in the business, and the corporation has paid from time to time, as this one hundred thousand dollars has accumulated the Territorial income tax on it. Now these gentlemen get together and they have a director's meeting to have distributed that hundred thousand dollars among themselves in the proportion they are entitled to, in proportion [208] to their stock holdings. They would claim their dividends as a deduction, as far as their individual income tax returns are concerned, on the ground that the corporation had already paid the taxes under the statute?

Mr. KAY: Objected to.

Mr. PETERS: I will withdraw the question.

Q. As a matter of departmental practice, has it not been the fact that dividends declared under those circumstances on which the tax has already been paid were claimed as deductions and allowed?

A. You say under those circumstances. If you mean the declaration of a dividend out of surplus, yes.

Q. Let me pursue the situation just a little further. And these two gentlemen agree among themselves that only one shall get a dividend, because the other wants his share of the surplus to remain in the business. He says you take your profits out and I will leave mine in. What is the difference between the hypotheses?

A. That is where I begin to differ with you. I don't think it is a dividend when it only goes to one man.

(Testimony of Harold C. Hill.)

Q. I see what is bothering you. Take a third hypothesis and say that instead of the remaining stockholder leaving his surplus in there he says to the other stockholder, "we will both take it out." "Well," says the first stockholder, "What are you [209] going to do? Are you going on your original contribution of capital?" "Oh, no," he says, "I will take this and claim it as a redemption and put it back into the company as representing my original contribution."

A. You are setting up a situation that did not occur.

Q. Quite right, but the situation as far as Lord and Black are concerned, they could have done it, couldn't they? Couldn't Mr. Lord and Mr. Black have got together and regularly declared a dividend of the entire surplus and both claim a deduction under the income tax law, and E. E. Black, Limited, have gone to the Treasurer's office and reduced it to his original contribution,—in this particular instance forty thousand dollars, and go to work and issue some more stock for the dividend he had received, and then increase it again before the Treasurer's office? If he had done that there would have been no taxes so far as Mr. Lord and Mr. Black were concerned, under those circumstances?

Mr. KAY: Objected to, as the Board is not concerned with what might have been done. We would require the taxpayer to advance the reasons why

(Testimony of Harold C. Hill.)

this procedure was not followed. If it had been followed, a much higher tax might have been paid. There may have been factors affecting such a procedure which would [210] not justify the procedure outlined by Judge Peters. Hence, for Judge Peters to put a question of what might have been done is purely hypothetical and not based on the evidence and facts in the case.

Mr. PETERS: Hasn't Mr. Kay asked the witness what this witness would have done if the case had come before him? All I am asking him is what the actual substance of the whole thing is?

Mr. ADAMS: I assume you are asking him what he would have done if that particular thing had come up.

The CHAIRMAN: Objection overruled.

Q. (Question read by the reporter.)

Mr. KAY: Objected to as duplicitous.

Mr. PETERS: Do you understand the question?

A. I understand what you are driving at all right.

Q. Let me put it this way. Would there be any tax liability as far as Mr. Lord is concerned under the following circumstances: The surplus of E. J. Lord, Limited is regularly distributed as a dividend to stockholders. E. J. Lord, Limited, or E. E. Black, Limited, its successor in name, goes to the Treasurer's office and reduces its capital stock to the amount of remaining capital; subsequently E. E. Black takes the amount he has received by way of

(Testimony of Harold C. Hill.)

this dividend and gain, contributing this to the capital stock, and likewise goes to the Treasurer's office and asks for an increase to meet the increased capital stock. Would there be [211] any income tax liability under the Territorial law so far as Mr. Lord is concerned?

Mr. KAY: Same objection, as it does not state the facts.

The CHAIRMAN: Objection overruled.

A. The first step in your case apparently being that the stockholders of E. J. Lord, Limited, should declare a dividend to all the stockholders?

Q. Yes, including E. J. Lord?

A. Stopping right there, that couldn't be, and I don't see how it could have been taxed under the Territorial law.

Q. And the subsequent acts do not effect the situation whatever?

A. I don't see how they could.

Q. What is the difference between that and the instant case?

A. In the instant case, the ultimate result perhaps is the same, but it is done in an entirely different manner, in that the corporation buys out one of the shareholders and pays that shareholder a price for its stock, a price far in excess of his original contribution, thereby netting him a profit.

Q. So as I understand it, due to the fact that Black did not participate in any dividend, that is the line of demarcation, so it converts the transac-

(Testimony of Harold C. Hill.)

tion entirely, according to your theory, into a sale by the original stockholder to the corporation from which [212] he has derived his profit?

A. Yes.

Q. And it is on the theory of that profit that you impose a tax?

A. That I would have imposed a tax.

Q. Will you tell the Board what kind of a dividend comes within the meaning of Section 1391,—that is the proviso?

A. Any publicly declared dividend,—or, to get away from the dividend, division of a share of the profits of the company which is taxable upon its income within the Territorial laws.

Q. And as a matter of fact, wasn't that just this, a division as between these two stockholders of the profits of that business and a distribution of the share of one to the one?

A. No, I don't think so.

Q. Is the trouble in your mind simply that Black did not get his too? If Black had got his too, it would have been a dividend?

A. I believe so.

Q. If Black had got his 40% and Lord his 60% it would have been a dividend?

Mr. KAY: You have a different situation. You have the situation of control creeping in there. You have a situation where one stockholder passes out of the picture.

(Testimony of Harold C. Hill.)

Mr. PETERS: What has that to do with the definition of the word "dividend"? [213]

Mr. KAY: It has a great deal to do as used in this provision of Section 1391. Dividend contemplates a distribution of earnings on stock that is returning.

Mr. PETERS: It would have been all right on the eve of the first of the year the dividend had been declared to Lord of 60% and on the second they had paid him the \$60,000., is that the idea?

Mr. KAY: That is a question of argument.

Q. Let's take this situation, Mr. Hill. Supposing this dividend had been declared on the first of the year, we will say on one day, and on the same day of the succeeding week the corporation went out and bought this stock of Lord's for the purpose of redemption. Would it change your mind any as to the character of this payment to Lord? That is Lord and Black got together and Black said to Lord, "You can take your 60% of the surplus out of here," then the corporation deals with Lord and pays him \$60,000., the original contribution, a week hence?

Mr. ADAMS: When Mr. Hill spoke of the division of the earnings, do you mean a division to one or prorata to all the stockholders?

A. Prorata to all the stockholders.

Q. As I understand, that is part of your mental processes in answering Mr. Kay was that this

(Testimony of Harold C. Hill.)

distribution of profits is equal among all the [214] stockholders of the corporation in accordance with their holdings?

A. Yes.

Mr. KAY: I object to this line of cross-examination which Judge Peters is going into. It is something that did not occur. We should confine ourselves to facts before the Board as to what did occur. These suppositious cases have no bearing on the facts as they already exist, and the application of law to those facts. We submit these suppositious cases have no bearing on the issues before this Board.

Mr. PETERS: I think Mr. Hill is trying to assist this Board, and my questions are put with the endeavor to assist this Board.

Mr. KAY: Judge Peters is presenting certain hypothetical situations. Those situations are not complete. He is not stating why this procedure was not followed. He is not giving reasons why E. J. Lord did not obtain a distribution along the lines as proposed by him. In other words, we are only being given a piece-meal hypothetical situation in each case, hence I urge again that this line of examination is of no help to the Board.

Mr. ADAMS: It is rather illuminating, I think.

Q. Let's assume something. Let's assume that legally a dividend can be paid to one stockholder by agreement between himself and all the other [215] stockholders. Assuming that is the law, would

(Testimony of Harold C. Hill.)

you change your opinion as to the assessability under the Territorial income tax law of any of the consideration paid to Mr. Lord?

Mr. KAY: Objected to as not based on any evidence in this case.

Q. You have never run against a dividend paid to one stockholder by agreement of the other stockholders?

A. No.

Q. You have never run against a case such as this, which by agreement of all the stockholders one stockholder gets his share of the surplus and he is clean out and the stock redeemed?

A. No, I don't know such a case.

Questions by Mr. Wrenn:

Q. And before you would have made an assessment in a case of this kind, you would have got an opinion from the Attorney-General's Department as to the law, would you not?

Mr. KAY: Objected to as immaterial.

The CHAIRMAN: Objection sustained.

Redirect Examination by Harold T. Kay, Esq.

Q. You referred to the case of Mineral Products and stated there had been plenty of losses. Were those losses claimed as losses by holders of the stock in Mineral Products in income tax returns made by [216] the stockholders?

A. As I recall, it was optional with the stockholders of Mineral Products whether they should

(Testimony of Harold C. Hill.)

surrender their stock for Magnesia Products or simply drop out of the picture. Those who took the Magnesia Products stock in exchange were not permitted to take a loss at that time. Those who dropped out naturally were given the benefit of the loss, that is the difference between what they paid for the stock and the total loss.

Q. In other words, they claimed losses which were allowed?

A. Yes.

Mr. KAY: That is the case for the Government.

Mr. WRENN: We reserved the right to examine Mr. Buchholtz on redirect. Evidently you don't care to recall him, but there are a few questions we should like to ask him.

GEORGE BUCHHOLTZ,

a witness for the Taxpayer, was recalled for further examination, and testified as follows:

Redirect Examination by Heaton L. Wrenn, Esq.

Q. You were asked on your cross examination by Mr. Kay whether there were any other dividends declared during the year 1930 other than the \$125,000, dividend [217] he called your attention to, and you said "no," in answer to that question. At my

(Testimony of George Buchholtz.)

request since that time have you refreshed your recollection on what occurred during that year?

A. Yes, I have.

Q. And after having refreshed your recollection, what is your answer to that question?

A. There was a dividend declared, but in my answer before I thought it was declared in 1931.

Q. And you have found that was declared in 1930?

A. Yes.

Q. What was the amount of that dividend and to whom was it paid?

A. Paid to Mr. Lord. I don't remember the amount now. It is in the minute book.

Q. A copy of which is on file and admitted in evidence?

A. Yes.

Recross Examination by Harold T. Kay, Esq.

Q. Will you refer to such records as may appear here in evidence in this case and show where in there was a dividend paid to Mr. Lord in 1930 and where the same appears in the records,—referring to what document do you base that statement of yours on?

A. I don't know what you mean on what document?

Q. You just made the statement on direct examination [218] that upon a reexamination of the records of your company you found that a dividend had been paid to Mr. Lord in 1930 other

(Testimony of George Buchholtz.)

than dividends referred to by you the other day?

A. In the minute book.

Q. I will ask you to refer to the records here in this case, and ask you to point out wherein it appears that a dividend was paid to Mr. Lord?

A. I am talking about a liquidating dividend. The word "dividend" does not apply from the reading of the language.

Mr. ADAMS: "Apply" or "appear"?

A. Does not appear.

Q. What does appear?

A. The first item here on the minutes of final settlement of E. J. Lord, the minutes of December 20, 1930.

Q. What appears there?

A. "Mr. E. E. Black moved that as Mr. E. J. Lord was willing to sell all his stock of E. J. Lord, Limited, the company was to redeem the 600 shares for which the company have to pay for the said shares in the following manner: (1) A sum of money equal to 60% of the net worth of the company as of December 31, 1929. (2) A sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929. (3) A sum of money equal to 40% of the amount to which Mr. E. J. Lord [219] may become liable for Federal and Territorial income taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares.

(Testimony of George Buchholtz.)

Mr. Lord agreed to give the company an option to purchase the above-mentioned stock to February 28, 1930, and to have an agreement drawn, signed by above parties, covering the above option, price and payments to be made, a copy of such agreement to be entered into the minute book. Mr. George Buchholtz seconded the motion which was carried unanimously.

Mr. Buchholtz moved that the company upon the exercise of the option cause its Articles of Association to be amended so that the name does not contain the name of 'E. J. Lord' or any words similar to that name."

Q. Does there appear in anything you have read a statement that a dividend had been paid to Mr. E. J. Lord?

A. Yes, by redemption of the stock.

Q. Was there anything specifically stated to the effect that a dividend had been paid to Mr. E. J. Lord?

A. No, the word "dividend" does not appear.

Q. That is the record of your company that you examined on reexamination and upon which you base your statement that a dividend had been paid to Mr. Lord in 1930?

A. That and the final settlement here. [220]

Q. What is that?

A. This is what I was referring to.

Q. Referring to what?

A. The company was to redeem the 600 shares.

(Testimony of George Buchholtz.)

Q. What document are you referring to?

A. Minutes of December 7, 1929.

Q. Entitled Taxpayers' Exhibit 38A?

A. That is right.

Q. Will you point out wherein that term "dividend" appears?

A. I said the word "dividend" does not appear.

Q. So when you used the term "dividend" in your direct examination in response to Mr. Wrenn's question, you were in error in using the term "dividend" were you not?

Mr. WRENN: Objected to as argumentative.

A. I didn't call that an error. I was referring to the liquidating dividend of these 600 shares.

Q. Then you want to qualify your original statement to mean that when you used the term "dividend" you mean "liquidating dividend," is that correct?

A. I suppose so.

Q. Referring to your trial balances, will you state whether in any of the trial balances in evidence in this case for the year 1930 there appears any statement showing that any dividends had been paid by E. J. Lord, Limited, other than the amount of \$25,000. in the year 1930? [221]

A. No; not under the heading of "dividends."

Reredirect Examination by Emil C. Peters, Esq.

Q. Your books do show the distribution to Mr. Lord of 60% of the surplus?

A. Yes, sir.

(Testimony of George Buchholtz.)

Q. And it was that that you refer to as a dividend?

A. Yes.

Rerecross Examination by Harold T. Kay, Esq.

Q. Is it not a fact that this distribution, that Judge Peters calls it, of 60% of the surplus is designated as payment or settlement for stock sold by Mr. E. J. Lord to E. J. Lord, Limited?

A. I would like to answer that question again. As this arose we first started paying Mr. Lord the final payment of \$250,000. It was in 1929, and a further payment was made a few months later upon the completion of the Louis Hind's job, and a third amount couldn't be paid until all these contracts were wound up. At the end of 1930 we had to have some sort of a temporary entry and that heading was called "E. J. Lord stock purchase account" in our books. I took this thing up at times with our auditor and I was first going to put the thing on the suspense account, because it was nothing but a temporary thing until the stock should be redeemed and the final payment was made.—
[222]

No. 2052

In the Supreme Court of the Territory of Hawaii

ON APPEAL FROM THE TERRITORIAL
BOARD OF EQUALIZATION.

In the Matter of the Income Tax Appeal of

EDMUND J. LORD

for the year ending December 31, 1930, First Taxa-
tion Division.

PETITION FOR APPEAL

and

AFFIDAVIT

[Endorsed]: Filed April 4, 1934 at 2:20 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

ROBERTSON & CASTLE,

312 Castle & Cooke Bldg.,

Honolulu, T. H.,

Attorneys for Petitioner.

[223]

[Title of Court and Cause.]

PETITION FOR APPEAL

To the Honorable Chief Justice and Associate Jus-
tices of the Supreme Court of the Territory of
Hawaii:

Comes now EDMUND J. LORD by his attorneys,
Robertson & Castle, and deeming himself aggrieved
by the decision and judgment of the above entitled
court in the above entitled cause, which judgment

was made and entered on the 25th day of January, 1934, pursuant to the opinion of the court theretofore rendered, and claiming that there are manifest and material errors to the damage of said Edmund J. Lord, which errors are specifically set forth in the assignment of errors filed herewith, to which reference is hereby made, respectfully prays that an appeal may be allowed him in the above entitled cause and that he be allowed to prosecute said appeal to the United States Circuit Court of Appeals for the Ninth Circuit in accordance [224] with the statutes in such cases made and provided; and your petitioner prays that an order be made fixing the amount of the bond to be given upon such appeal.

And your petitioner further prays that the Clerk of the Supreme Court of the Territory of Hawaii be directed to send to the United States Circuit Court of Appeals for the Ninth Circuit, a transcript of the record, proceedings and papers in this cause, together with the evidence and exhibits taken herein, all duly authenticated, for the correction of the errors so complained of, and that a citation may issue.

Your petitioner further shows that the decision and judgment of the above entitled cause was rendered in an appeal from the Territorial Board of Equalization, and that the value in controversy, ex-

clusive of interest and costs, exceeds \$5,000, as appears by the record herein.

Dated: Honolulu, T. H., this 4th day of April, 1934.

ROBERTSON & CASTLE,
By NORMAN NEWMARK,
Attorneys for Petitioner.

[225]

[Title of Court and Cause.]

AFFIDAVIT

Territory of Hawaii

City and County of Honolulu—ss.

ALFRED L. CASTLE, being first duly sworn, deposes and says that he is a member of the firm of Robertson & Castle, attorneys for the above named Edmund J. Lord, and duly authorized to make this affidavit on his behalf; that he has read the foregoing Petition for Appeal, knows the contents thereof; that the matters and things therein set forth are true; and that the value in controversy in the above entitled matter exceeds \$5,000, exclusive of interest and costs.

ALFRED L. CASTLE.

Subscribed and sworn to before me this 4th day of April, 1934.

[Seal]

FLORENCE LEE,
Notary Public, First Judicial Circuit,
Territory of Hawaii.

[226]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS

[Endorsed]: Filed April 4, 1934 at 2:20 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

ROBERTSON & CASTLE,

312 Castle & Cooke Bldg.,

Honolulu, T. H.

Attorneys for Edmund J. Lord.

[227]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS

Comes now the above named Edmund J. Lord and files the following assignment of errors upon which he will rely in the prosecution of the appeal herewith petitioned for in the said cause to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment of this court made and entered on the 25th day of January, 1934.

Assignment No. 1

The Supreme Court of the Territory erred in failing to rule that that part of the consideration received by Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, over and above his original capital contribution, which represented his theretofore undivided interest in the accumulated earnings, profits and surplus of said corporation, and which was paid out of such earnings, profits and surplus, upon which a [228] Territorial income tax

had been assessed and paid, was received as dividends and was exempt from taxation under the provisions of Section 1391, R. L. 1925.

Assignment No. 2

The Supreme Court of the Territory erred in failing to rule that that part of the consideration received by Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, over and above his original capital contribution, which was paid out of accumulated corporate earnings, profits and surplus upon which a territorial income tax had been assessed and paid, was exempt from taxation under the provisions of Section 1391, R. L. 1925.

Assignment No. 3

If some part of the consideration received by said Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, was subject to taxation despite the provisions of Section 1391, Revised Laws, 1925, then the Supreme Court of the Territory of Hawaii erred in failing to rule that the tax could be assessed only on the difference between the value of said stock as of January 1, 1930, and the amount which he received therefor.

WHEREFORE, said Edmund J. Lord prays that the judgment of the Supreme Court of the Territory of Hawaii be reversed and the cause remanded with directions to set aside the proposed assess-

ment, and for such other or further orders or relief as to the Court may seem just and proper.

Dated: Honolulu, T. H., this 4th day of April, 1934.

ROBERTSON & CASTLE,

Attorneys for Edmund J. Lord.

Service of a copy of the foregoing assignment of errors is hereby admitted this 4th day of April, 1934.

H. R. HEWITT,

Attorney General.

[229]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL AND FIXING
AMOUNT OF BOND

[Endorsed]: Filed April 4, 1934 at 2:45 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[230]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL AND FIXING
AMOUNT OF BOND

The petition of Edmund J. Lord for an appeal to the United States Circuit Court of Appeals for the Ninth Circuit, dated the 4th day of April, 1934, from the final judgment of this Court dated the 25th day of January, 1934, is hereby granted and the appeal is allowed; and the amount of the bond is hereby fixed in the sum of \$250.00.

Dated: Honolulu, T. H., this 4th day of April, 1934.

[Seal]

ANTONIO PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii. [231]

[Title of Court and Cause.]

CITATION ON APPEAL

[Endorsed]: Filed April 4, 1934 at 3:00 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[232]

[Title of Court and Cause.]

CITATION ON APPEAL

To THE TERRITORY OF HAWAII and
HARRY R. HEWITT, its Attorney General:
GREETING:

You are hereby cited and admonished to be and appear in the United States Circuit Court of Appeals for the Ninth Circuit, to be held in the City of San Francisco, State of California, within thirty days from the date hereof, pursuant to an order allowing an appeal from the Supreme Court of the Territory of Hawaii in a suit wherein Edmund J. Lord is appellant, to show cause, if any there be, why the judgment rendered against said appellant should not be corrected and why speedy justice should not be done to the said appellant on that behalf.

WITNESS the Honorable Charles Evans Hughes, [233] Chief Justice of the Supreme Court of the United States of America, this 4th day of April, 1934.

[Seal]

ANTONIO PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii.

Receipt of a copy of the foregoing Citation is hereby admitted this 4th day of April, 1934.

H. R. HEWITT,
Attorney General of the Territory of Hawaii.

[234]

[Title of Court and Cause.]

BOND ON APPEAL

[Endorsed]: Filed April 4, 1934 at 2:46 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[235]

[Title of Court and Cause.]

BOND ON APPEAL

KNOW ALL MEN BY THESE PRESENTS:
That EDMUND J. LORD, as Principal, and
UNITED STATES FIDELITY AND GUARAN-
TY COMPANY, as Surety, are held and firmly
bound unto THE TERRITORY OF HAWAII in
the full and just sum of Two Hundred and Fifty
Dollars (\$250.00) to be paid to the said The Terri-
tory of Hawaii, to which payment, well and truly to

be made, the above named parties bind themselves, their respective heirs, executors, administrators, successors and assigns, firmly by these presents.

WHEREAS, in the above entitled cause and Court, an appeal from the judgment heretofore therein rendered has been taken and allowed to the United States Circuit Court of Appeals for the Ninth Circuit,

NOW, THEREFORE, if the said principal shall [236] prosecute said appeal with effect and pay all costs if he fails to sustain said appeal, then this obligation shall be void; otherwise it shall remain in full force and effect.

IN WITNESS WHEREOF the said EDMUND J. LORD, Principal, and UNITED STATES FIDELITY AND GUARANTY COMPANY, Surety, have caused these presents to be executed this 4th day of April, 1934.

(Signed) EDMUND J. LORD,

Principal.

UNITED STATES FIDELITY AND
GUARANTY COMPANY,

[Seal] By HERMAN LUIS,
Its Attorney-in-Fact,
Surety.

Approved as to form and amount of bond and sufficiency of surety.

[Seal] (Signed) ANTONIO PERRY,
Chief Justice, Supreme Court of
the Territory of Hawaii. [237]

[Title of Court and Cause.]

PRAECIPE

[Endorsed]: Filed April 4, 1934 at 3:01 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

ROBERTSON & CASTLE,

312 Castle & Cooke Bldg.,

Honolulu, T. H.,

Attorneys for Edmund J. Lord.

[238]

[Title of Court and Cause.]

PRAECIPE

To ROBERT PARKER, ESQUIRE, Clerk of the
Supreme Court of the Territory of Hawaii:

You will please prepare a transcript of the record
in the above entitled cause to be filed in the office
of the Clerk of the United States Circuit Court of
Appeals for the Ninth Circuit and include in said
transcript the following:

1. Territorial income tax return of E. J. Lord
dated June 18, 1931, together with notice of change
of assessment dated June 19, 1931 pasted thereon,
and schedule attached thereto;

2. Notice of Appeal from Assessment dated June
18, 1931;

3. All exhibits;

4. Transcript of evidence taken before the Board
of Equalization, excluding therefrom the arguments
of counsel beginning on page 194 and continuing to
the end;

5. Decision of the Territorial Board of Equal-
ization dated the 20th day of January, 1932; [239]

6. Appeal and Notice of Appeal dated January 29, 1932, from the Territorial Board of Equalization to the Supreme Court of the Territory of Hawaii;

7. Affidavit of Charles T. Wilder, Chairman of the Board of Equalization, dated February 1, 1932;

8. Decision of the Supreme Court of the Territory of Hawaii, dated the 2nd day of December, 1933;

9. Judgment of the Supreme Court of the Territory of Hawaii, dated January 25, 1934;

10. Petition for appeal and affidavit;

11. Assignment of errors;

12. Order allowing appeal and fixing amount of bond;

13. Citation;

14. Bond on appeal;

15. This praecipe;

16. All orders enlarging time to docket cause.

You will annex to and transmit with the record the original citation issued in said cause, originals of all orders enlarging time to docket cause and your certificate under seal stating in detail the cost of the record and by whom paid, in compliance with Rule 14 of the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: Honolulu, T. H., this 4th day of April, 1934.

(s) ROBERTSON & CASTLE,
Attorneys for Edmund J. Lord.

Service of a copy of the foregoing Praeceptum is hereby admitted this 4th day of April, 1934.

(s) H. R. HEWITT,

Attorney General of the Territory of Hawaii.

[240]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

[Endorsed]: Filed April 20, 1934 at 2:30 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[241]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

Upon the application of Appellant above named,
and good cause appearing therefor,

IT IS HEREBY ORDERED, pursuant to Section 1 of Rule 16 of the United States Circuit Court of Appeals for the Ninth Circuit, that Appellant above named and the Clerk of this Court be and they are hereby allowed up to and including the 2nd day of June, 1934, within which to file the record and transcript and docket said cause with the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: Honolulu, T. H., April 20, 1934.

[Seal]

ANTONIO PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii.

Attest:

ROBERT PARKER, JR.,
Clerk.

[242]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

[Endorsed]: Filed May 12, 1934 at 10:30 o'clock
A. M. Robert Parker, Jr., Clerk Supreme Court.

[243]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

Upon the application of Appellant above named,
and good cause appearing therefor,

IT IS HEREBY ORDERED, pursuant to Section 1 of Rule 16 of the United States Circuit Court of Appeals for the Ninth Circuit, that Appellant above named and the Clerk of this Court be and they are hereby allowed up to and including the 15th day of July, 1934, within which to file the record and transcript and docket said cause with the Clerk

of the United States Circuit Court of Appeals for
the Ninth Circuit.

Dated: Honolulu, T. H., May 12th, 1934.

[Seal]

A. PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii.

Approved:

W. B. PITTMAN,
Attorney General.

Attest:

ROBERT PARKER, JR.,
Clerk.

[244]

[Title of Court and Cause.]

STIPULATION AS TO CONTENTS OF
TRANSCRIPT OF RECORD

[Endorsed]: Filed June 28, 1934 at 9:00 o'clock
A. M. Robert Parker, Jr., Clerk Supreme Court.

WILLIAM B. PITTMAN,
Attorney General,
Honolulu, Territory of
Hawaii.

ROBERTSON & CASTLE,
312 Castle & Cooke Bldg.,
Honolulu, T. H. [318]

[Title of Court and Cause.]

STIPULATION AS TO CONTENTS OF
TRANSCRIPT OF RECORD

IT IS HEREBY STIPULATED AND AGREED by and between the TERRITORY OF HAWAII, appellee, and EDMUND J. LORD, appellant, that the transcript of record to be certified to and filed in the United States Circuit Court of Appeals for the Ninth Circuit, pursuant to the appeal heretofore allowed herein, shall exclude the following exhibits:

Tax Assessor's Exhibit "A";

Tax Payers' Exhibits 1, 2, 4, 6-a, to 6-f, 7, 8-a-b-c, 10, 11, 12, 13, 17, 32 and 36.

IT IS FURTHER STIPULATED that the Clerk of Court shall omit the aforesaid exhibits from the record to be filed on appeal without the necessity of the filing of an amended praecipe, and that this stipulation shall take effect upon the approval thereof by Honorable Antonio Perry, Chief Justice of the above entitled court, or upon the approval of either of the Associate Justices thereof.

Dated: Honolulu, T. H., this 27 day of June, 1934.

TERRITORY OF HAWAII,
By MONTGOMERY E. WINN,
Its First Deputy Attorney
General.

EDMUND J. LORD,
By ROBERTSON & CASTLE,
His Attorneys.

Approved:

[Seal]

ANTONO PERRY,
Chief Justice, Supreme Court
of Hawaii.

[Title of Court and Cause.]

CLERK'S CERTIFICATE.

Territory of Hawaii

City and County of Honolulu—ss.

I, ROBERT PARKER, JR., Clerk of the Supreme Court of the Territory of Hawaii, by virtue of the petition for appeal filed April 4, 1934, the original whereof is attached to the foregoing transcript of record, being pages 223 to 226, both inclusive, and in pursuance to the praecipe filed April 4, 1934, copy whereof is attached to the foregoing transcript of record, being pages 238 to 240, both inclusive, and in pursuance to the stipulation filed June 28, 1934, the original whereof is attached to the foregoing transcript of record, being pages 318 to 319, both inclusive.

DO HEREBY TRANSMIT to the Honorable United States Circuit Court of Appeals for the Ninth Circuit, the foregoing transcript of record, being pages 1 to 222, both inclusive, pages 235 to 237, both inclusive, pages 245 to 317 both inclusive, and I CERTIFY the same to be full, true and correct copies of the record, entries, opinions, minutes, exhibits and final judgment, which are now on file in the office of the Clerk of the Supreme Court of the Territory of Hawaii, in the above entitled cause, Supreme Court No. 2052.

I DO FURTHER CERTIFY that the original assignment of errors, filed April 4, 1934, with acknowledgment of service of a copy by H. R. Hewitt,

Attorney General, being pages 227 to 229, both inclusive, the original order allowing appeal and fixing amount of bond, filed April 4, 1934, being pages 230 to 231, both inclusive, the original citation on appeal, filed April 4, 1934, with acknowledgment of service of a copy thereof by H. R. Hewitt, Attorney General, being pages 232 to 234, both inclusive of the foregoing transcript of record, are herewith returned.

I LASTLY CERTIFY that the cost of the foregoing transcript of record is \$160.55, and the said amount has been paid by Messrs. Robertson & Castle, attorneys for E. J. Lord. [320]

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the seal of the Supreme Court of the Territory of Hawaii, at Honolulu, City and County of Honolulu, Territory of Hawaii, this 29th day of June, 1934.

[Seal]

ROBERT PARKER, JR.,
Clerk of the Supreme Court of the
Territory of Hawaii. [321]

No. 7543

In the United States Circuit Court of Appeals for
the Ninth Circuit.

APPEAL FROM THE SUPREME COURT OF
THE TERRITORY OF HAWAII
EDMUND J. LORD,

Appellant,

vs.

TERRITORY OF HAWAII,

Appellee.

STIPULATION AS TO PRINTING OF
RECORD

ROBERTSON & CASTLE,
312 Castle & Cooke Bldg.,
Honolulu, T. H.,

Attorneys for Appellant.

WILLIAM B. PITTMAN, ESQ.,
Attorney General,
Territory of Hawaii,

Attorney for Appellee.

[Title of Court and Cause.]

STIPULATION AS TO PRINTING OF
RECORD

IT IS HEREBY STIPULATED by and between the respective parties hereto, that in printing the record in the above entitled cause, the Clerk shall omit therefrom the following documents and papers:

Tax Assessor's Exhibits B to B-14, inclusive, being photostatic copies of trial balances of E. J. Lord, Limited, (or E. E. Black, Limited), for the months of November and December, 1929, and for the months of January to December 1930, said exhibits being found on pages —— to —— in the transcript of record certified to the above entitled court by the Clerk of the Supreme Court of the Territory of Hawaii;

Taxpayers' Exhibits 18 to 22, inclusive, being territorial income tax returns of E. J. Lord, Limited, for income earned during the years 1926 to 1929, inclusive, and of E. E. Black, Limited, for income earned during the year 1930, said exhibits being found on pages —— to —— in the transcript of record certified to the above entitled court by the Clerk of the Supreme Court of the Territory of Hawaii; and

Taxpayers' Exhibits 23 to 27, inclusive, being receipts for income taxes paid by E. J. Lord, Limited, and E. E. Black, Limited, for income earned during the years 1926 to 1930, inclusive, said exhibits being found on pages —— to —— in the

transcript of record certified to the above entitled court by the Clerk of the Supreme Court of the Territory of Hawaii.

Dated: Honolulu, T. H., this 27th day of June, 1934.

TERRITORY OF HAWAII,
By MONTGOMERY E. WINN,
Its First Deputy Attorney
General.

EDMUND J. LORD,
By ROBERTSON & CASTLE,
His Attorneys.

Approved:

ANTONIO PERRY,
Chief Justice of the Supreme Court
of the Territory of Hawaii.

Justice of the United States Court
of Appeals for the Ninth Circuit.

[Endorsed]: Filed July 6, 1934. Paul P. O'Brien,
Clerk.

[Endorsed]: No. 7543. United States Circuit Court of Appeals for the Ninth Circuit. Edmund J. Lord, Appellant, vs. Territory of Hawaii, Appellee. Transcript of Record. Upon Appeal from the Supreme Court of the Territory of Hawaii.

Filed July 6, 1934.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

